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IN THE

Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-1565

ASSOCIATED GAS DISTRIBUTORS,
Petitioner,

v.

FEDERAL POWER COMMISSION,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

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April 26, 1976

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ASSOCIATED GAS DISTRIBUTORS

Member Companies

Atlanta Gas Light Company
The Brooklyn Union Gas Company
Central Hudson Gas and Electric Corporation
Consolidated Edison Company of New York, Inc.
Elizabethtown Gas Company
Fitchburg Gas and Electric Light Company
Long Island Lighting Company
New Jersey Natural Gas Company
New York State Electric & Gas Corporation
North Carolina Natural Gas Corporation
Philadelphia Electric Company
Philadelphia Gas Works
Piedmont Natural Gas Company, Inc.
Public Service Company of North Carolina, Inc.
Rochester Gas and Electric Corporation
UGI Corporation
Washington Gas Light Company

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

Petitioner Associated Gas Distributors (AGD) respectfully prays that a writ of certiorari be issued to review the judgment and opinion of the United States Court of Appeals for the District of Columbia Circuit entered in this case on January 28, 1976.

OPINION BELOW

The opinion of the Court of Appeals has not yet been reported. It is attached hereto as Appendix A.

JURISDICTION

This Court's jurisdiction is invoked under 28 U.S.C. §1254(1) and Section 19(b) of the Natural Gas Act, 15 U.S.C. §717r(b).

STATUTORY PROVISIONS INVOLVED

The relevant portions of the Natural Gas Act, 15 U.S.C. §717, *et seq.*, are set out in Appendix C of this Petition.

STATEMENT OF THE CASE

This case involves judicial review of two F.P.C. rate increase orders[1] which are representative of a large class of rate increases authorized by the F.P.C. during the period from April 1973 to June 1974.[2] The rate orders at bar were sought and received by Mobil Oil Corporation (Mobil) and Continental Oil Company (Continental).

The purchasers of gas in these two sales are interstate pipeline companies[3] which sell gas at wholesale to gas distribution companies including members of the Associated Gas Distributors (AGD) group of Petitioners. AGD is an ad hoc group of natural gas distribution companies providing gas utility service to consumers in the major market centers of

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[1] These orders, together with related F.P.C. orders denying rehearing thereof, are included as Appendix B of this Petition.

[2] *See*, note 33, *infra*, and accompanying text.

[3] In the Continental sale, the purchaser is Tennessee Gas Pipe Line Company. In the Mobil sale, the purchaser is Texas Eastern Transmission Corp.

the eastern seaboard.[4] Individually, these companies are legally responsible for maintaining adequate natural gas utility service at reasonable rates within their respective franchise areas. As a result of the decision here on review, and F.P.C. action in a series of comparable orders affecting a large number of other interstate gas sales to pipelines serving AGD companies, the price of gas sold to AGD companies and, in turn, sold to their gas consumers, has been substantially increased. Likewise, these orders have failed to elicit any additional gas supply for AGD's consumers. Accordingly, AGD's interest here is that of protecting its consumers from any unlawful or unjustified increase in the cost of natural gas and their right to an adequate gas supply.

A. Proceedings Before the Federal Power Commission

1. The Two Tier Producer Rate System and Opinion No. 639.

Commencing with its landmark decision in the *Permian Basin Area Rate Cases*,[5] the F.P.C. had established by the close of 1971 a system of area ceiling price regulation for all jurisdictional sales of natural gas by producers in each of the gas production areas of the contiguous 48 states.[6] In each area, the scheme of rate design was determined on a basis of a full adjudicatory hearing or a rulemaking proceeding in which all interested parties had a full opportunity to file initial and reply comments on all matters under consideration by the F.P.C. A common element adopted by the F.P.C. in each of its area pricing orders was a two-tier rate structure. Thus, gas previously developed and dedicated to the interstate market (designated as "flowing gas") received one price while new gas

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[4]The members of AGD are listed on the inside cover of this Petition.

[5]*Permian Basin Area Rate Proceeding*, 34 FPC 159 (1965), *aff'd. sub nom. Permian Basin Area Rate Cases (Continental Oil Co. v. FPC)*, 390 U.S. 747 (1968).

[6]See cases cited at Appendix A, pp. 8-9 (Dissenting Opinion).

dedicated after the institution of the rate proceeding received a higher, incentive-oriented price. The purpose of this higher price was (a) to reflect the higher current and future exploration and development costs as contrasted with the lower costs extant when the flowing gas was dedicated, (b) to gear the incentive features in the new gas price to the relative need for gas, and (c) to encourage the dedication of new gas reserves to the interstate market.

On January 28, 1972, a number of pipelines and distributors filed a petition to initiate a fresh review of prices in the Appalachian and Illinois Basin areas. The petitioners requested a "third tier" price of 50 cents per Mcf for new gas reserves dedicated to the interstate market after February 1, 1972. The F.P.C. issued a notice summarizing this petition in F.P.C. Docket No. R-371 on June 19, 1972. The notice encouraged comments and the public was advised that the Commission would consider termination of the moratoria provisions applicable to that area and "such revisions of §154.107, 154.108... as may be found to be in the public interest."[7]

On December 12, 1972, the Commisison issued its Opinion No. 639[8] denying petitioners' request for the establishment of a third price ceiling. The F.P.C. then addressed the two-tier or rate vintaging feature of the area rate system—a subject not mentioned in the initial petitions, the F.P.C.'s notice, or any comments filed pursuant to that notice—and declared not only that vintaging should be eliminated in this area but in all production areas.[9] To this end, the Commission stated that its previous area rate orders

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[7]Rate ceilings were established in that area pursuant to Order No. 411, 44 FPC 1112 (1970). Sections 154.107 and 154.108 are codifications of the rate orders for the Appalachian-Illinois Basin areas, respectively, 18 CFR §§154.107 and 154.108. As in all prior area rate decisions, Order No. 411 contained a two-tier rate design.

[8]*Area Rates for the Appalachian-Illinois Basin Areas,* Opinion No. 639, Docket No. R-371, 48 FPC 1299(1972), *aff'd, sub nom. Shell Oil Co. v. FPC,* 491 F.2d(5th Cir. 1974).

[9]*Id* at 1309.

should be "literally and strictly applied," i.e., if a flowing gas contract expires by its terms, and a new contract is executed, sales under such contract will be governed by the ceiling price applicable to new or second vintage contracts. Thus, by way of dictum, the Commission purported in its Appalachian and Illinois Basin order to carve out a major exception to the two-tier scheme of price regulation governing all other producing areas. On appeal, this feature of Opinion No. 639 was upheld as a permissible interpretation of previous area rate orders.[10]

2. The Instant Proceedings

The present cases were initiated by separate F.P.C. filings by Mobil and Continental. On December 21, 1972, Mobil sought permission to abandon certain service to Shell Oil Company (Shell). The application stated that Mobil's contract with Shell had expired and that a new contract had been executed with Texas Eastern Transmission Corporation, the pipeline to which Shell had previously delivered the gas received under the now-expired Mobil-Shell contract. Approval of the Mobil-Texas Eastern sale was sought in a companion application; in that application, Mobil sought a rate equal to the 25 cents per Mcf area ceiling for "new" of second vintage gas established for the Texas Gulf Coast Area.[11] As authority for its collection of the higher, "new gas" ceiling rate, Mobil relied on F.P.C. Opinion No. 639.

The Continental filing was made on February 15, 1973. There, Continental submitted a "renewal contract," i.e., a gas sales agreement under which it agreed to continue service rendered to Tennessee Gas Pipeline Company under a contract which had expired by its terms. Continental's rate filing likewise sought permission to collect the higher, new gas rate

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[10] *Shell Oil Co. v. FPC*, 491 F.2d 82 (5th Cir. 1974).

[11] The record does not disclose the price previously collected by Mobil. However, the ceiling price for first vintage sales from this area was 19 cents per Mcf.

on the basis of Opinion No. 639.

AGD filed timely petitions to intervene in each of these proceedings. In due course, each of the producers' requests were granted and AGD filed applications for rehearing. AGD argued in these applications (a) the application of the new gas price to these sales was not justified by evidence in these cases nor by the dictum of Opinion No. 639, (b) that the two price system adopted throughout the Commission's area rate orders could not be undone without an evidentiary predicate, and (c) that the Commission's duty to protect the consumer requires that some assurance of a gas supply *quid pro quo* be obtained before rate increases are allowed for sales already dedicated to the interstate market. In its rehearing orders, the Commission cited Opinion No. 639 as dispositive of the producers' right to charge the new gas rate for the sales in question.[12] The Commission thus refused to undertake any independent review of the circumstances surrounding the instant sales to determine whether these rate increases were likely to yield any corresponding increase in gas supply.

B. Proceedings in the Court Below

On appeal, the Court of Appeals for the D.C. Circuit upheld the Commission's action in these cases in a 2-1 decision. The majority opinion held that Opinion No. 639 contained adequate findings, based on substantial evidence, to support the Commission's departure from the two-tier or vintaging concept insofar as the renewal contracts are concerned.

> Opinion No. 639 findings did in fact include detailed discussion of national gas supply, area gas drilling and production activities, intrastate competition for new gas, the need for deep gas exploration, comparison with costs of supplemental gas, and changes in costs of finding and producting new gas supplies. A major fact finding, pointing

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[12] *See*, Appendix B.

> toward the failure of vintaging, was that the exploratory gas well count in the area had been 97 wells in 1968 and that within one year after the issuance of Order No. 411 in 1970, applying the vintaging concept to the area, the exploratory gas well count dropped to 47 wells.[13]

The dissenting opinion found a lack of substantial evidence in Opinion No. 639 to support the orders here. The dissent regarded as crucial the absence of evidence in Opinion No. 639 supplying a nexus between the application of the new gas price to renewal contracts and the Commission's goal of using price as an incentive for improved gas supply. The contrasting views of the majority and dissent are illustrated in the following excerpt from the dissenting opinion.

> Under the plan projected by Opinion No. 639, the "new" price is not restricted to gas produced from new wells developed in that field; rather, all gas from the field would command the "new" price, including gas discovered, developed and dedicated long ago. Like the Fifth Circuit, the most I can say is that it is merely "conceivable" that the expectations of Opinion No. 639 will become a reality; like my colleagues, I cannot say with any degree of assurance that it actually will. In this milieu, there is, at least for me, a call for evidence resolving affirmatively the critical question whether the Commission's policy of pricing "old" gas at the "new" rate is promising enough as an incentive to survive the test of reasonableness. (footnotes omitted)[14]

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[13] Appendix A, p. 7.

[14] Appendix A, p. 18 (Dissenting Opinion).

REASON FOR GRANTING THE WRIT

1. The orders now before this Court signal a significant shift in the direction of F.P.C. rate regulation of gas producers. If allowed to stand, the policy reflected in these orders will in time erase the two-tiered structure of rate regulation which the Commission has consistently applied since the inauguration of group ratemaking for gas producers.[15] Commencing with the Commission's 1965 *Permian* decision,[16] the adoption of separate prices for new and flowing gas was seen as a reasonable device by which to balance the interests of consumer protection against excessive prices, on the one hand, and the need for a price high enough to provide the incentive for finding more expensive gas supplies on a current and prospective basis.

The two-tier structure was affirmed by this Court "on the basis of substantial evidence that a two-price rate structure will both provide a useful incentive to exploration and prevent excessive profits."[17] The Court specifically approved the Commission's reasoning

> "that excessive producer profit could be minimized only if the rate for flowing gas were derived from the most precise available evidence of actual historical costs."[18]

It recognized that the price fixed for "old" gas was relatively low "since price could not serve as an incentive, and since any price above average historical costs, plus an appropriate return, would merely confer windfalls."[19] Following its

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[15] *See*, Opinion No. 639, 48 FPC at 1310.

[16] *Permian Basin Area Rate Case, supra*, note 5.

[17] *Id*, at 798.

[18] *Id*, at 802.

[19] *Id*, at 797.

adoption in *Permian* in 1965, the Commission consistently employed the two-tier system in each of the other area rate proceedings which comprised its overall producer regulatory system.[20]

Nothing in the orders here demonstrates the need to abandon the two-tier system insofar as the instant sales are concerned. The application of the higher, new gas price to the Mobil and Continental contracts was not predicated on any evidence or findings that, as a result of the rate increase, further drilling would be undertaken or additional gas reserves dedicated.[21] Nor did these producers claim that the perviously-applicable flowing gas price was less than compensatory for the service rendered. The only discernible effect of the Commission's orders is that higher prices were received by the producers. The sole justification given by the Commission for allowing these rate increases was its Opinion No. 639 determination to interpret literally the vintaging provisions contained in area rate orders.[22]

Opinion No. 639 furnishes neither a legal nor factual basis for modifying the pre-existing two-tier rate structure applicable to the instant sales. On its face, Opinion No. 639 is a Commission ruling on issues raised with respect to rates in the Appalachian and Illinois Basin Areas. The proceeding which led to Opinion No. 639 was initiated by a public notice advising, *inter alia*, that the F.P.C. would consider such revisions of Sections 154.107, 154.108 [the pre-existing rate orders for the Appalachian and Illinois Basin Area]" . . . as may be found to be in the public interest." On the merits, the F.P.C. in Opinion No. 639 denied the rate relief requested by various parties with respect to sales made from the Appalachian and Illinois Basin Area. The Commission then

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[20] *See*, case cited at pp. 8-9, Appendix A (Dissenting Opinion).

[21] *See*, Appendix B.

[22] *Ibid.*

turned to the question of "price vintaging"—a phrase denoting the two-tier rate structure and a subject not mentioned in its notice or in any comments. In this gratuitous discussion, the F.P.C. stated that vintaging would be eliminated in all production areas by permitting the seller to charge the higher new gas price whenever a new contract was executed after the new gas division date and after expiration of the old contract.[23] This policy, the F.P.C. indicated, would be carried out "by interpretation of the specific language used in setting vintage rates.[24] Thus, the F.P.C. seized on the fact that the distinction between flowing gas and new gas had fortuitously been made on the basis of *contract date* rather than *service commencement date* as a device by which to abandon the two-tier system without following the procedures necessary to modify rates previously determined to be just and reasonable, i.e., those required by Section 5 of the Natural Gas Act.[25]

Despite its ingenuity, the F.P.C.'s literal interpretation theory is legally unsound. A literal interpretation of a provision which is inconsistent with its purpose must be avoided whenever the language can be construed consistent with its purpose.[26] The purpose of the two-tier price system is to provide an incentive to exploration while at the same time preventing excess producer profits on older, low cost service.[27] The F.P.C.'s literal interpretation, as applied in these cases, yields a price for old or flowing gas which is well

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[23] 48 FPC at 1309.

[24] 48 FPC at 1310. The two-tier structure created in the several area rate orders defined the applicability of the separate prices for flowing gas and new gas in terms of *contract* date rather than date of initiation of service. The choice of the contract date as the basis for the purpose of facilitating subsequent rate changes. *See, Texas Gulf Coast Area Rate Proceeding,* 45 FPC 674, 713(1971), *aff'd. on remand sub nom. Public Service Comm'n v. FPC,* 516 F.2d 746 (D.C. Cir. 1975).

[25] *See,* Appendix C.

[26] *See, Haggar v. Helvering,* 308 U.S. 389, 394 (1940); *Ozawa v. U.S.,* 260 U.S. 178, 194 (1922).

[27] *Permian Basin Area Rate Cases, supra,* at 798.

above the average-historical-cost-plus-return basis on which the flowing gas price was fixed. The orders below thus distort the purpose of the two-tier system and confer a classic windfall on the producers. What the F.P.C. termed an interpretation of its earlier rate orders was, in truth, a major revision thereof. Unquestionably, the F.P.C. had no legal power in its *Appalachian and Illinois Basin Area Rate Order* (Opinion No. 639) to revise the just and reasonable rate structure prescribed in other proceedings for the Texas Gulf Coast and Other Southwest Areas.

Nor did the Commission supply any factual predicate in Opinion No. 639 which would rationalize its orders in these cases. Its factual explanation was limited to the following statement:

> Vintaging operates to discourage development of the full productive capacity of acreage committed to the interstate market, for even though such developmental drilling is undertaken at current costs, gas production obtained thereby is priced at the *lower* of two rates, when it is the *higher* of the two that is Commission-designed to provide the incentive for development of additional gas supplies.[28]

Assuming this finding were valid,[29] it bears no relationship to the Mobil or Continental service covered by the instant orders. Neither producer claimed any intention to conduct developmental drilling in order to realize the full productive capacity of the fields in question. F.P.C.'s abandonment of

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[28] 48 FPC at 1309.

[29] No such assumption is justified. Both area rate orders covering the instant sales provided for escalations in the flowing gas price to reflect "increased drilling costs, well rehabilitation, equipment repair and replacement revenues from flowing gas as a source of funds for new investments," *Other Southwest Area Rate Proceeding*, 46 FPC at 900-918, N.23; *aff'd. sub nom. In re Other Southwest Area Rate Cases (Shell Oil Co. v.FPC)* 484 F.2d 469 (5th Cir. 1973), *cert. denied* 417 U.S. 973 (1974); *Texas Gulf Coast Area Rate Proceeding*. 45 FPC at 707-708.

the two-tier rate system is these cases should not be condoned by this Court. If major revisions in the ceiling rates applicable to older, flowing gas service are necessary, or if vintaging should be abolished, the Commission should be required to so find in a proceeding where those issues can be fully addressed by all parties. A policy so fundamental to the established scheme of producer regulation should not be undone through *post hoc*, "literal" interpretations.

2. The instant orders raise serious questions concerning the Commission's accountability to the nation's gas consumers in a period of acute gas shortage. In enacting the Natural Gas Act, it was

> "the intention of Congress that natural gas shall be sold in interstate commerce for resale for ultimate public consumption for domestic, commercial, industrial, or any other use at the lowest possible reasonable rate consistent with the maintenance of adequate service in the public interest."[30]

The two themes of consumer protection from excessive rates and adequate gas service run throughout this Court's rulings involving F.P.C. rate orders.[31] Each of these principles is seriously prejudiced by the orders here.

The relationship of these orders to the issue of consumer rate protection has to do first, with the *quantum of justification* given for these rate increases. The F.P.C.'s apparent purpose in Opinion No. 639 was to provide natural gas producers with additional funds to finance development drilling for the benefit of the interstate market.

This is plainly a legitimate ratemaking *purpose* in this

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[30] *Atlantic Refining Co. v. Public Service Comm'n*, 360 U.S. 378, 388 (1959).

[31] *See, FPC v. Hope Natural Gas Co.*, 320 U.S. 591 (1944), *Permian Basin Area Rate Cases*, 390 U.S. 747 (1968).

time of nationwide gas shortage. But this purpose is not reflected in what the Commission has done here. Neither in Opinion No. 639 nor in the orders at bar did the Commission require any showing that the revenues derived from the producers' rate increases would be devoted to gas supply-enhancing activity. The *justification* for these rate increases is simply the execution of a new contract upon the expiration of the old. Whether the producers (whose primary product is *oil*) will choose to use these revenues for additional gas development is the problem. Certainly it is reasonable to expect that Mobil and Continental will elect to invest these revenues in activities other than gas exploration where their profits are not regulated.

The majority opinion in the court below upheld the F.P.C. because "it is not illogical to believe" that additional gas revenues will lead to an increased supply.[32] Such an approach to the Commission's ratemaking power is at war with the consumer protection purpose of the Natural Gas Act. The mere fact that additional revenues are thereby conferred on gas (and oil) producers in a time of gas shortage does not establish the justness and reasonableness of an F.P.C. rate order. An increase of *any* amount would qualify under such standard.

The precedent value of these cases is also pertinent to the issue of F.P.C. accountability to the gas consumer. The orders before the Court are representative of a group of not less than 52 such rate orders entered by the F.P.C. in reliance on Opinion No. 639.[33] These 52 rate orders cover a total of 224 separate renewal contract filings made by gas producers, i.e., many of the orders are "omnibus" rulings granting increases on a series of contracts. No computation has been

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[32] Appendix A, p. 10.

[33] AGD has intervened in those 52 separate FPC rate proceedings based on Opinion No. 639 in which the rate increases affected pipelines serving the eastern seaboard. Other cases involving increases to other pipelines have been processed but no count has been made.

made of the cumulative dollar impact of these increases. Nonetheless, it is safe to assume that the impact runs into the millions *and is still accumulating.* Moreover, the policy first adopted in Opinion No. 639 has been carried over in subsequent F.P.C. orders (now pending before this Court on writs of certiorari) revising the new gas ceiling prices.[34] These orders magnify the dollar impact of the Opinion No. 639 policy. Whereas Opinion No. 639 purported to authorize increases in the range of 4 to 15 cents per Mcf (depending on the applicable area price and the rate level previously collected), F.P.C. Opinion No. 699-H allows escalations in the range of 30 cents per Mcf.

Finally, the gas supply consequences of the instant orders and Opinion No. 639 are adverse insofar as the consumer is concerned. In response to the gas supply crisis, the F.P.C. has issued various rate orders in recent years which approve arrangements allowing producers to retain or earn revenues above the otherwise applicable just and reasonable ceiling in return for a commitment by the producer to explore for and/or sell additional gas to the interstate market. In the *Southern Louisiana Area Rate Cases,*[35] producers were allowed to "work off" some $150 million in excess charges by dedicating new gas reserves to the interstate market. In the same case, producers were allowed to earn flowing gas rate increases by dedicating additional gas reserves to the interstate market.[36] More recently, the F.P.C. has allowed pipeline-producers to increase rates charged their customers for company-produced gas in return for a commitment by the company to use the added revenue for gas exploration.[37]

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[34] *See, Shell Oil Company v. FPC,* 520 F2d 1061 (5th Cir. 1975). AGD's Petition for Certiorari of this ruling is pending at No. 75-1308.

[35] 46 FPC 86, 147-148 (1971), *aff'd. sub nom. Mobil Oil Corporation v. FPC* 417, U.S. 283 (1974).

[36] *Id,* at 143.

[37] *Panhandle Eastern Pipe Line Company,* Opn. No. 626, 48 FPC 518 (1972).

Further, in the *Tennessee Bastian Bay* case[38] the Commission allowed certain producers to retain revenues relating to past excessive charges on condition that a specific volume of new gas reserves be dedicated to the Tennessee pipeline system within a specified period. In Opinion No. 639 and in the instant orders, the F.P.C. inexpliciably ignored the opportunity to fashion a similar gas supply *quid pro quo* remedy. If the F.P.C. were to use the millions of dollars of revenues involved here as leverage to induce additional interstate gas sales, the supply impact could be truly significant. The failure to do so leaves the consumer interest unprotected both in terms of adequate gas service and excessive, unjustified rates.

CONCLUSION

For the reasons set forth above the Court should grant the petition for certiorari to review the judgment and opinion of the U. S. Court of Appeals for the District of Columbia Circuit.

Respectfully submitted,

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April 26, 1976

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[38] *Tennessee Gas Peipline Company, a Division of Tenneco Inc., et al.*, Opinion No. 667, 50 FPC 1194 (1973).

Appendix A

Notice: This opinion is subject to formal revision before publication in the Federal Reporter or U.S. App. D.C. Reports. Users are requested to notify the Clerk of any formal errors in order that corrections may be made before the bound volumes go to press.

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 73-1647

PUBLIC SERVICE COMMISSION FOR THE STATE OF NEW YORK, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT

CONTINENTAL OIL COMPANY, MOBIL OIL CORPORATION, PHILLIPS PETROLEUM COMPANY, ASSOCIATED GAS DISTRIBUTORS, INTERVENORS

No. 73-1793

ASSOCIATED GAS DISTRIBUTORS, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT

PHILLIPS PETROLEUM COMPANY, CONTINENTAL OIL COMPANY, MOBIL OIL CORPORATION, INTERVENORS

No. 73-1794

ASSOCIATED GAS DISTRIBUTORS, PETITIONER

v.

FEDERAL POWER COMMISSION, RESPONDENT

MOBIL OIL CORPORATION, INTERVENOR

Petition for Review of Orders of the Federal Power Commission

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Decided January 27, 1976

Richard A. Solomon, with whom *Peter H. Schiff*, was on the brief for petitioner in 73-1647 and 73-1793.

Frederick Moring, with whom *Richard G. Morgan* and *Thomas C. Watson*, were on the brief for petitioner in No. 73-1794.

John R. Staffier, Attorney, Federal Power Commission, for respondent. *Leo E. Forquer*, General Counsel, Federal Power Commission, *George W. McHenry, Jr.*, Solicitor, *Richard A. Oliver* and *A. Lee Wallace*, Attorneys, Department of Justice, were on the brief for respondent.

Tom Burton, for intervenor Continental Oil Company.

Carroll L. Gilliam, with whom *Tom P. Hamill* and *Phillip R. Ehrenkranz*, were on the brief for intervenor Mobil Oil Corporation.

John L. Williford, entered an appearance for intervenor Phillips Petroleum Company.

Before: ROBINSON and ROBB, *Circuit Judges* and MARKEY,* *Chief Judge*, United States Court of Customs and Patent Appeals

Opinion for the Court filed by *Chief Judge* MARKEY.

Dissenting opinion filed by *Circuit Judge* ROBINSON.

MARKEY, *Chief Judge, United States Court of Customs and Patent Appeals*: These appeals present the question of whether the Federal Power Commission (Commission) may permit application of previously established "new" gas rates to flowing natural gas ("old" gas) sold pursuant to a new contract which replaces an expired contract. We answer in the affirmative.

The Facts

The seeds for these appeals were sown by the issuance of the Commission's Opinion No. 639.[1] The Commission announced in No. 639 that the language of previous area rate orders, which had established the criterion for "old" gas rates and "new" gas rates ("vintaging"), would be literally and strictly applied. Specifically, the Commission announced that

> [t]he wording of Order No. 411, and all other Commission area rate orders or opinions of similar import, stating that 'old' gas rates will be applicable to 'gas sold pursuant to a contract dated prior to October 8, 1969' will be literally and strictly applied. If a gas contract dated prior to October 8, 1969, terminates, and the purchaser and seller enter into a new contract, gas sales under the new contract will be governed by the applicable pricing provisions relating to 'gas sold pursuant to a contract dated after

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* Sitting by designation pursuant to 28 U.S.C. § 293(a).

[1] *Area Rates for Appalachian and Illinois Basin Areas*, 48 FPC 1299 (1972), *reh. denied*, 49 FPC 361 (1973), *aff'd sub nom., Shell Oil Co. v. F.P.C.*, 491 F.2d 82 (5th Cir. 1974).

> October 7, 1969.' . . . In time this will result in the elimination of a two-price system, a result we believe intended by the original authors of vintaging and a result we wholeheartedly endorse.

On applications for hearing the Commission in Opinion No. 639-A clarified this decision, saying (49 FPC 364)

> the new gas ceiling may be applied upon execution of a new contract for deliveries of gas previously certified and dedicated to the interstate market under a contract *which has expired by its own terms.* [Emphasis in original.]

Under the vintaging concept, employed since 1960, "new" gas had been considered as limited to gas from newly discovered fields. Hence the rate established in the original contract for gas from a particular field applied to gas from additional wells in that field and to later contracts for gas from that field, i.e., all gas from that field was "old" gas. The Commission's present interpretation means that "new" gas rates may be applied without regard to whether the contract covers gas from a newly discovered field or whether it replaces an expired contract for currently flowing gas.

On December 21, 1972, Mobil Oil Company (Mobil) applied for permission to abandon certain natural gas sales to Shell Oil Company (Shell). The application indicated that Mobil's sales contract with Shell had expired by its own terms and that a new contract had been negotiated with Texas Eastern Transmission Company (Texas Eastern). Approval of the latter sale was requested in a related application in which Mobil indicated that it would accept an initial rate equal to the area ceiling for "new" gas established in Commission Opinion No. 595 [2] for the Texas Gulf Coast Area. As authority for allowing it to

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[2] *Area Rate Proceeding (Texas Gulf Coast Area)*, 45 FPC 674, *reh. denied*, 46 FPC 826 (1971).

collect the "new" gas rate, Mobil cited Commission Opinion No. 639. Associated Gas Distributors (AGD) sought and was permitted to intervene. A hearing was held and on April 16, 1973, the Commission found[3] the proposed abandonment to be "permitted by the public convenience and necessity." The Commission also granted Mobil a temporary certificate authorizing sale under the Texas Eastern contract at the area "new" gas rate. AGD's request for rehearing was denied and a petition to this court (No. 73-1794) to review the Commission's order followed.

Contemporaneously, the Commission issued a notice that Continental Oil Company, Getty Oil Company, and Phillips Petroleum Company had filed requests for rate increases, the first two in the Other Southwest Area and Phillips in the Texas Gulf Coast Area. AGD and the Public Service Commission of the State of New York (PSCNY) were permitted to intervene. In each case the oil company had apparently entered into a new contract after the expiration of a prior contract. The Commission's order of April 27, 1973, cited Opinion No. 639 as controlling and granted the requested rates. Following denial of a request for rehearing, this court was petitioned, separately by PSCNY (No. 73-1647) and by AGD (No. 73-1793), to review the Commission's order.

The three appeals were consolidated for briefing and argument before us.

Issue

The substantive issue is whether the Commission's orders, permitting application of the "new" gas rates established in prior area rate orders, are authorized. The appealed orders involve individual implementations of the Commission's prior decision to discontinue, gradually and as individual contracts expire, the use of the

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[3] 49 FPC 1009, *reh. denied*, 49 FPC 1411 (1973).

two-price (vintaging) system. That decision, first announced by interpretative rule in Opinion No. 639, was reviewed and approved as "rational, reasonable, and therefore fully permissible" in *Shell Oil Co.* v. *F.P.C.*, 491 F.2d 82, 89 (5th Cir. 1974).[4]

OPINION

The Commission's natural gas regulation efforts, in the short view, appear plagued by conflicting goals. While guarding against artificially inflated rates, it must simultaneously assure a rate schedule sufficient to encourage vigorous development of new gas sources assuring maintenance of an adequate gas supply. In the long view, increased supply may be considered a major prerequisite to reduced rates and the apparent conflict in goals may be seen to evaporate.

To prompt the search for and development of new gas deposits, the Commission incorporated into its area rate schedules a two-price system, referred to as the concept of "vintaging." See generally, *Placid Oil Co.* v. *F.P.C.*, 483 F.2d 880 (5th Cir. 1973), *aff'd sub nom. Mobil Oil Corp.* v. *F.P.C.*, 417 U.S. 283, 94 S.Ct. 2328, 41 L.Ed.2d 72 (1974); *Austral Oil Co.* v. *F.P.C.*, 428 F.2d 407 (5th Cir.), *cert. denied*, 400 U.S. 950, 91 S.Ct. 244, 27 L.Ed.2d 257 (1970). Conceived in 1960, the vintaging mechanism first appeared in a completed rate order in 1965. *Per-*

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[4] We decline the invitation to treat *Shell* as binding under the doctrine of res judicata or collateral estoppel. The parties here are not identical to or in privity with those in Shell. Nor are the causes of action identical. They arise from different contracts and different Commission orders. *Commissioner* v. *Sunnen*, 333 U.S. 591 (1948). We note, however, that petitioners here were intervening parties in *Shell* and that much of petitioners' expanded argument here was absent from the proceedings below on the orders herein appealed and from the presentations made in *Shell*.

mian Basin Area Rate Proceeding, 34 FPC 159 (1965), *reh. denied*, 34 FPC 1068 (1965), *remanded sub nom. Skelly Oil Co.* v. *F.P.C.*, 375 F.2d 6 (10th Cir. 1967), on rehearing, 375 F.2d 35 (1967), *modified sub nom. Permian Basin Area Rate Cases*, 390 U.S. 747, 88 S.Ct. 1344; 20 L.Ed.2d 312 (1968). The two-price vintaging policy was viewed from the outset as a *temporary* measure. *Statement of General Policy No. 61-1*, 24 FPC 818 (1960).

Unhappily, the Commission's creation, vintaging, failed to achieve the desired results. Opinion No. 639 contains "substantial evidence" to support that finding of failure, 15 U.S.C. § 717r(b). As the court said in *Shell* (491 F.2d at 85 n.8), "no fact findings are disputed." The Opinion No. 639 findings did in fact include detailed discussion of national gas supply, area gas drilling and production activities, intrastate competition for new gas, the need for deep gas exploration, comparison with costs of supplemental gas, and changes in costs of finding and producing new gas supplies. A major fact finding, pointing toward the failure of vintaging, was that the exploratory gas well count in the area had been 97 wells in 1968 and that within one year after the issuance of Order No. 411 in 1970, applying the vintaging concept to the area, the exploratory gas well count dropped to 47 wells.

In Opinion No. 639 the Commission recognized the failure and stated:

> We believe vintaging to be an anachronism which we should now move to eliminate. Vintaging operates to discourage development of the full productive capacity of acreage committed to the interstate market, for even though such developmental drilling is undertaken at current costs, gas production obtained thereby is priced at the *lower* of two rates, when it is the *higher* of the two that is Commission-designed to

provide the incentive for development of additional gas supplies. [Original emphasis.]

* * * *

Any change in vintage rates would require a modification by us of rates already determined to be just and reasonable. Many of these determinations are under judicial review and should not now be altered by the Commission. We are free, however, to effect one change in the application of vintaging concepts by interpretation of the specific language used in setting vintage rates, and we now do so.

Appellate review of Opinion No. 639 was thorough in *Shell* and we are in full agreement with the conclusions reached in that case. Petitioners here, as in *Shell*, do not attack the fact findings in Opinion 639, but only the conclusion reached by the Commission therein with respect to vintaging.

We particularly note the following in *Shell* (491 F.2d at 89-90):

A caveat is appropriate at this point. In regard to vintaging, today we are approving FPC's interpretation of certain regulations. We do not reach the question of whether FPC may altogether discontinue the use of vintaging. Rather in each future rate order the Commission must continue to produce substantial evidence to support each essential element of the proposed rate structure. In re Permian Basin Area Rate Cases, [390 U.S. 747, 88 S.Ct. 1344, 20 L.Ed.2d 312 (1968)]. Certainly the absence or presence of vintaging must be regarded as an essential element.

Though we concur completely in the quoted "caveat," we note that the instant appeals do not involve an area rate order per se or a "proposed rate structure." The question of whether the "new" gas rates themselves are "just and reasonable" under 15 U.S.C. § 717d(a) is not

before us. Presumably, substantial evidence to support those rates is present in the previously issued applicable area rate orders. Those orders are not in dispute here and the present case does not involve an area rate proceeding with all of the protracted fact finding efforts, over a period of years, which such a proceeding entails.

We share the concern, expressed in argument before us and by our dissenting brother, that the increased rates permissible under the Commission's new interpretation of area rate schedules may lead to increased gas prices without triggering the desired exploration for additional gas deposits. In *Shell* (491 F.2d at 89), the court recognized the same argument:

> But FPC's new interpretation of the vintaging provisions will produce a contrary result, we are told. With "new" and flowing gas at the same price level, the producers will have no incentive to find more gas because they can reap windfall profits by selling cheap flowing gas at the higher rate formerly reserved for "new" gas. If FPC required the producers to show higher costs or new production to justify the higher rate, then FPC would be acting rationally. But it is irrational only to raise gas rates with no *quid pro quo* required. The producers will not find increased production to be in their best interest, and, as NYPSC puts it, they will "take the money and run."

The Fifth Circuit, however, went on to say (*Id.*):

> It is also conceivable, however, that a departure from vintaging will serve to increase gas production. In Opinion 639 the Commission stated it believes that vintaging actively discourages new drilling on acreage already committed to the interstate market. If a producer has signed a contract before the division date, all the gas he producers [sic] during the contract's life will receive the low "old gas" price. Even if he drills new wells at current costs, the

> "new" gas he discovers and produces will be priced as "old" gas, on the basis of historical costs computed in a year long since gone by. Since costs seem to rise inexorably with the passage of time, new drilling will become less attractive as the contract ages. For example, we think it quite likely that a producer operating under a 1964 contract may have little incentive to find expensive 1974 gas only to sell it at bargain 1964 rates. But if he can raise his prices to a uniform rate for both "new" and "old" gas when the old contract expires and a new one is signed, he might be more inclined to drill new wells.
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> If the higher rates do stimulate production, the extra increment for flowing gas will supply needed additional capital for exploration and drilling. Precedent, moreover, supports the view that FPC does not necessarily create an irrational windfall when it includes in the price of flowing gas an increment for further exploration and development. We approved in *SoLa II* [*Placid Oil Co.* v. *F.P.C.*, 483 F.2d 880 (5th Cir. 1973), *aff'd sub nom.*, *Mobil Oil Corp.* v. *F.P.C.*, 417 U.S. 283, 94 S.Ct. 2328, 41 L.Ed.2d 72 (1974)] a rate structure with just such an increment.

No one can say with certainty that additional gas revenues will lead to an increased gas supply. It is apparent, however, that without sufficient revenue to support exploration for new deposits and further development of old deposits, an increased quantum of such activity is unlikely. The evidentiary factors discussed in Opinion No. 639 support that conclusion. The Commission's action, in modifying its earlier interpretation of its own vintaging mechanism, followed a pragmatic, non-doctrinaire approach based on its experience and expertise. It is not illogical to believe that removal of impediments can result in revival of the impeded activity. It is well, also, to recognize, as did the court in *Austral Oil, supra,* (at note 46) that:

> The gas industry is different from metropolitan transit in that it requires a constant infusion of entrepreneurship of the highest order if even basic public needs are to be satisfied. * * * On the other hand, we count upon persons who carefully weigh investment risks for our supply of natural gas. We think the Commission here, having calculated the dangers involved in allowing the gas supply to lapse, and the probabilities that its estimates might be too low, is justified in having added the small noncost factors it thought were necessary. It found that it needed to do so to protect the public interest and not to assure any rights of gas producers.

As noted in *Placid*, *supra*, the distinction between "old" gas and "new" gas is artificial. We agree with the holding in *Shell* that the Commission cannot be charged with error because it chose a literal and strict interpretation of particular language in preference to another possible interpretation. The Commission's interpretation of what constitutes "new" gas, and application of that interpretation in the present cases, were reasonable actions falling within its authority.

The orders under review are affirmed.

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SPOTTSWOOD W. ROBINSON, III, *Circuit Judge*, dissenting: Seven years ago the Supreme Court prescribed standards by which orders of the Federal Power Commission are to be measured on judicial review.[1] The order must not abuse or exceed the Commission's authority.[2] Every essential element of the order must be supported by substantial evidence.[3] Every factor pertinent to protection of the public as well as the private interests at stake must be given "reasoned consideration."[4] And, as the Court more recently emphasized, "application of [these]

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[1] "First, [the reviewing court] must determine whether the Commission's order, viewed in light of the relevant facts and of the Commission's broad regulatory duties, abused or exceeded its authority. Second, the court must examine the manner in which the Commission has employed the methods of regulation which it has itself selected, and must decide whether each of the order's essential elements is supported by substantial evidence. Third, the court must determine whether the order may reasonably be expected to maintain financial integrity, attract necessary capital, and fairly compensate investors for the risks they have assumed, and yet provide appropriate protection to the relevant public interests, both existing and foreseeable. The court's responsibility is not to supplant the Commission's balance of these interests with one more nearly to its liking, but instead to assure itself that the Commission has given reasoned consideration to each of the pertinent factors." *Permian Basin Area Rate Cases, (Continental Oil Co.* v. *FPC)*, 390 U.S. 747, 791-792, 88 S.Ct. 1344, 1372-1373, 20 L.Ed.2d 312, 350 (1968). See also *Mobil Oil Corp.* v. *FPC*, 417 U.S. 283, 307-308, 94 S.Ct. 2328, 2345-2346, 41 L.Ed.2d 72, 95, (1974); *Public Serv. Comm'n* v. *FPC*, 167 U.S.App.D.C. 100, 107, 511 F.2d 338, 345 (1975); *Macdonald* v. *FPC*, 164 U.S.App.D.C. 248, 255-256, 505 F.2d 355, 362-363 (1974); *Memphis Light, Gas & Water Div.* v. *FPC*, 164 U.S.App.D.C. 156, 161, 504 F.2d 225, 230 (1974).

[2] See note 1 *supra*.

[3] See note 1 *supra*.

[4] See note 1 *supra*.

three criteria of judicial review of Commission orders is primarily the task of the courts of appeals." [5]

This court has consistently endeavored to honor that responsibility. It has set aside orders reflecting misuses of Commission power.[6] It has rejected orders without sufficient foundation in the evidence.[7] It has overturned orders omitting "reasoned consideration" of relevant factors.[8] Today, however, the court takes a different course; it affirms orders contemptuous of all three of the criteria governing review. I respectfully dissent.

The Natural Gas Act[9] requires just and reasonable

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[5] *Mobil Oil Corp.* v. *FPC, supra* note 1, 417 U.S. at 309-310, 94 S.Ct. at 2346, 41 L.Ed.2d at 95-96. See also *Permian Basin Area Rate Cases (Continental Oil Co.* v. *FPC), supra* note 1, 390 U.S. at 766, 88 S.Ct. at 1359, 20 L.Ed.2d at 335-336; *Cities of Fulton* v. *FPC*, —— U.S.App.D.C. ——, ——, 512 F.2d 947, 951 (1975); *Public Serv. Comm'n* v. *FPC, supra* note 1, 167 U.S.App.D.C. at 107, 511 F.2d at 345; *Macdonald* v. *FPC, supra* note 1, 164 U.S.App.D.C. at 256, 505 F.2d at 363.

[6] *E.g., Arkansas Power & Light Co.* v. *FPC*, —— U.S.App.D.C. ——, ——, 517 F.2d 1223, 1236-1237 (1975); *Moss* v. *FPC*, 164 U.S.App.D.C. 1, 11-12, 502 F.2d 461, 471-472 (1974), *cert. granted*, 422 U.S. 1006, 95 S.Ct. 2627, 45 L.Ed.2d 668, *cert. denied*, 422 U.S. 1020, 95 S.Ct. 2642, 45 L.Ed.2d 680 (1975).

[7] *E.g., Arkansas Power & Light Co.* v. *FPC, supra* note 6, —— U.S.App.D.C. at ——, 517 F.2d at 1232-1236; *Macdonald* v. *FPC, supra* note 1, 164 U.S.App.D.C. at 255-258, 505 F.2d at 362-365; *Memphis Light, Gas & Water Div.* v. *FPC, supra* note 1, 164 U.S.App.D.C. at 162-167, 504 F.2d at 231-236.

[8] *E.g., Public Serv. Comm'n* v. *FPC, supra* note 1, 167 U.S.App.D.C. at 108-117, 511 F.2d at 346-355; *Macdonald* v. *FPC, supra* note 1, 164 U.S.App.D.C. at 255-258, 505 F.2d at 362-365.

[9] Act of June 21, 1938, ch. 556, 52 Stat. 821, as amended, 15 U.S.C. §§ 717 *et seq.* (1970).

rates for all gas regulable by the Commission [10] and declares any other rate unlawful.[11] Prices which producers charge pipelines for gas destined for resale in the interstate market are subject to these commands,[12] and producer-rate orders challenged as unjust or unreasonable must survive application of the judicial-review standards.[13] The rates set by the orders before us lack both evidentiary underpinning [14] and reasoned consideration,[15] and consequently on the administrative record were beyond the authority of the Commission.[16]

I

The Natural Gas Act effectuates a congressional purpose to hold prices for gas subject to its provisions "at the lowest possible reasonable rate consistent with the maintenance of adequate service in the public interest." [17] Obviously the public interest is served by an ample supply of gas as well as by low prices. So, within a "zone of

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[10] Natural Gas Act § 4(a), 15 U.S.C. § 717c(a) (1970).

[11] *Id.*

[12] *FPC* v. *Texaco, Inc.*, 417 U.S. 380, 394, 94 S.Ct. 2315, 2324-2325, 41 L.Ed.2d 141, 154 (1974); *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672, 676-685, 74 S.Ct. 794, 795-801, 98 L.Ed. 1035, 1044-1049 (1954).

[13] See note 1 *supra*.

[14] Part II *infra*.

[15] Part III *infra*.

[16] See text *infra* at notes 123-124.

[17] *Atlantic Ref. Co.* v. *Public Serv. Comm'n*, 360 U.S. 378, 388, 79 S.Ct. 1246, 1253, 3 L.Ed.2d 1312, 1319 (1959), quoting original § 7(c) of the Act, 52 Stat. 825 (1938), which, though later eliminated, remains a fundamental purpose. 360 U.S. at 388 n.7, 79 S.Ct. at 1253 n.7, 3 L.Ed.2d at 1319 n.7.

reasonableness," [18] the Commission may properly "employ price functionally in order to achieve relevant regulatory purposes; it may, in particular, take fully into account the probable consequences of a given price level for future programs of exploration and production." [19] The statutory goals of adequate supply and fair prices remain harmonious since "[t]he Commission's responsibilities include the protection of future, as well as present, consumer interests," [20] and the "price is thus just and reasonable . . . because it results in satisfactory programs of exploration, development and production." [21]

There is, however, a problem that frequently accompanies inclusion within the price of a noncost factor intended as an incentive to exploration for or development of new sources of gas. The problem is separation of situations wherein higher prices thus constituted are genuine inducements to greater exploratory and developmental effort from situations wherein such prices are not likely to have that effect, and so are apt to do no more than provide financial windfalls to producers. Reasonableness of a rate, so evident when the rate is prudently calculated to bring forth new stores of gas, disappears as that result becomes improbable. Manifestly, protection of the public interest calls for more than an offering of the higher price to the two divergent classes of cases indiscriminately.

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[18] *FPC* v. *Natural Gas Pipeline Co.*, 315 U.S. 575, 585, 62 S.Ct. 736, 742-743, 86 L.Ed. 1037, 1049 (1942).

[19] *Permian Basin Area Rate Cases (Continental Oil Co.* v. *FPC)*, *supra* note 1, 390 U.S. at 797, 88 S.Ct. at 1375-1376, 20 L.Ed.2d at 353.

[20] *Id.* at 798, 88 S.Ct. at 1376, 20 L.Ed.2d at 353-354.

[21] *Id.* at 796, 88 S.Ct. at 1375, 20 L.Ed.2d at 352. See also *FPC* v. *Texaco, Inc.*, *supra* note 12, 417 U.S. at 388-390, 94 S.Ct. at 2321-2323, 41 L.Ed.2d at 151-152; *Mobil Oil Corp.* v. *FPC*, *supra* note 1, 417 U.S. at 316-320, 94 S.Ct. at 2349-2352, 41 L.Ed.2d at 99-102.

When the problem was first addressed administratively, the Commission solved it by utilizing the technique known as price vintaging. That response emerged ten years ago in the first area gas-rate order—covering production in the Permian Basin [22]—when the Commission substituted area ratemaking for case-by-case determination of producer rates on the traditional cost-of-service basis.[23] The Commission settled on a higher price as an incentive to exploration and development, and vintaging as the means of limiting the higher price to activity of that character.[24] So it was that vintaging became a standard feature of gas-rate orders for years to come.

In its Permian Basin order, the Commission adopted two maximum area prices, differentiated by a date approximating the time at which programs specifically directed toward exploration for and development of new

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[22] *Permian Basin Area Rate Proceeding*, (Opinion No. 468), 34 F.P.C. 159 (1965), *rehearing denied* (Opinion No. 468-A), 34 F.P.C. 1068 (1965), *remanded sub nom. Skelly Oil Co.*, v. *FPC*, 375 F.2d 6 (10th Cir. 1967), *on rehearing*, 375 F.2d 35 (1967), *rev'd in part sub nom. Permian Basin Area Rate Cases (Continental Oil Co.* v. *FPC)*, *supra* note 1.

[23] For judicial discussions of the shift from individual to area ratemaking for the natural gas industry, see *Permian Basin Area Rate Cases (Continental Oil Co.* v. *FPC)*, *supra* note 1, 390 U.S. at 755-765, 88 S.Ct. at 1353-1359, 20 L.Ed.2d at 329-334; *Mobil Oil Corp.* v. *FPC*, *supra* note 1, 417 U.S. at 301-306, 94 S.Ct. at 2342-2345, 41 L.Ed.2d at 91-94; *FPC* v. *Texaco, Inc.*, *supra* note 12, 417 U.S. at 387-389, 94 S.Ct. at 2321-2322, 41 L.Ed.2d at 150-152. See also *Phillips Petroleum Co.* (Opinion No. 388), 24 F.P.C. 537 (1960), *rehearing denied*, 24 F.P.C. 1008 (1960), *aff'd sub nom. Wisconsin* v. *FPC*, 112 U.S.App.D.C. 369, 303 F.2d 380 (1961), *aff'd*, 373 U.S. 294, 83 S.Ct. 1266, 10 L.Ed.2d 357 (1963); Statement of General Policy No. 61-1, 24 F.P.C. 818 (1960).

[24] *Permian Basin Area Rate Proceeding* (Opinion No. 468), *supra* note 22, 34 F.P.C. at 185-189.

sources of natural gas became widely possible.[25] One price, the higher of the two, established the ceiling for "new" gas-well gas—gas produced independently of oil[26] and dedicated to the interstate market after the division

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[25] The genesis of the two-tier pricing system in area rate-making has been described by the Supreme Court as follows:

> [T]he Commission concluded that price could usefully serve as an incentive to exploration and production only if it were computed according to the method by which gas is produced. Natural Gas produced jointly with oil is necessarily a relatively unimportant by-product. The value of oil-well gas is on average only one-seventeenth that of the oil with which it is produced. See 34 F.P.C. at 322. It cannot be separately sought or independently produced; its production is effectively restricted by state regulations intended to encourage the conservation of oil. Accordingly, the supply of oil-well gas is, as the examiner observed, "almost perfectly inelastic." *Id.*, at 323.
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> On the other hand, gas-well gas is produced independently of oil, and of state restrictions on oil production. More important, the Commission found that a separate search can now be conducted for gas reservoirs; cumulative drilling experience permits at least the larger producers to direct their programs of exploration and development to the search for gas. The supply of gas-well gas is therefore relatively elastic, and its price can meaningfully be employed by the Commission to encourage exploration and production. The Commission reasoned that a higher maximum rate for gas-well gas dedicated to interstate commerce after the approximate moment at which a separate search became widely possible would provide an effective incentive. Correspondingly, the Commission adopted a relatively low price for all other natural gas produced in the Permian Basin, since price could not serve as an incentive, and since any price above average historical costs, plus an appropriate return, would merely confer windfalls.

Permian Basin Area Rate Cases (Continental Oil Co. v. *FPC), supra* note 1, 390 U.S. at 796-797, 88 S.Ct. at 1375-1376, 20 L.Ed.2d at 352-353 (footnotes omitted).

[26] See note 25 *supra*.

date.[27] The "new" price was calculated from data reflecting the costs of finding and producing gas-well gas in the years prior to the division date.[28] The lower price setting the level for "old" gas—all other gas, including that produced from fields already in operation—was derived from historical costs of producing gas-well gas in the area.[29]

Thus "[t]he Commission's use of separate sources of data for the two rates permitted the creation of a price differential between them without the inclusion of noncost components." [30] The Permian Basin order incorporated the Commission's specific finding that vintaging "holds out a reward to encourage producers to engage in further exploration and development while preventing

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[27] *Permian Basin Area Rate Cases (Continental Oil Co.* v. *FPC), supra* note 1, 390 U.S. at 759-760 88 S.Ct. at 1355-1356, 20 L.Ed.2d at 332. The division date was January 1, 1961. *Id.*

[28] *Id.* at 800-801, 88 S.Ct. at 1377-1378, 20 L.Ed.2d at 355-356.

[29] *Id.* at 801-802, 88 S.Ct. at 1377-1378, 20 L.Ed.2d at 356.

[30] *Id.* at 803, 88 S.Ct. at 1378-1379, 20 L.Ed.2d at 1356-1357. The Commission "computed the two area maximum prices directly from costs of service, without allowances for noncost factors"; its price differential was "the product of differences in the time periods and geographical areas for which costs were computed and not of noncost additives to cost components." *Id.* at 799-800, 88 S.Ct. at 1376-1377, 20 L.Ed.2d at 354-355. See, however, *id.* at 814-815 & n.98, 88 S.Ct. at 1384-1385 & n.98, 20 L.Ed.2d at 363 & n.98. It is, of course, now clear that the Commission may properly include, within a zone of reasonableness, noncost incentives to exploration, development and production of new sources of natural gas. *E.g., Mobil Oil Corp.* v. *FPC, supra* note 1, 417 U.S. at 316-321, 94 S.Ct. at 2349-2352, 20 L.Ed.2d at 99-102; *Permian Basin Area Rate Cases (Continental Oil Co.* v. *FPC), supra* note 1, 390 U.S. at 796-798, 815 & n.98, 88 S.Ct. at 1375-1376, 1384-1385 & n.98, 20 L.Ed.2d at 352-354, 363 & n.98.

excess and unnecessary revenues from the sale of gas developed at a period when there was no special exploratory activity directed to gas discovery." [31] In accepting unqualifiedly the concept of vintaging, the Supreme Court adverted particularly to the Commission's finding, "on the basis of substantial evidence, that a two-price rate structure will both provide a useful incentive to exploration and prevent excessive producer profits." [32] The Court noted, too, the Commission's reasoning "that excessive producer profits could be minimized only if the rate for flowing gas were derived from the most precise available evidence of actual historical costs," [33] and that the price fixed for "old" gas was relatively low "since price could not serve as an incentive, and since any price above average historical costs, plus an appropriate return, would merely confer windfalls." [34]

This multiple-price methodology—"vintaging"—has been a common element of rate design in a lengthy series of area ratemaking orders since the one promulgated for the Permian Basin in 1965.[35] As 1972 drew to a close,

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[31] *Permian Basin Area Rate Proceeding* (Opinion No. 468), *supra* note 22, 34 F.P.C. at 186.

[32] *Permian Basin Area Rate Cases (Continental Oil Co.* v. *FPC), supra* note 1, 390 U.S. at 798, 88 S.Ct. at 1376, 20 L.Ed. 2d at 354. See also *FPC* v. *Texaco, Inc. supra* note 12, 417 U.S. at 388-390, 94 S.Ct. at 2321-2323, 41 L.Ed. at 151-152.

[33] *Permian Basin Area Rate Cases (Continental Oil Co.* v. *FPC), supra* note 1, 390 U.S. at 802, 88 S.Ct. at 1378, 20 L.Ed. 2d at 356.

[34] *Id.* at 797, 88 S.Ct. at 1375-1376, 20 L.Ed.2d at 353.

[35] *Permian Basin Area Rate Proceeding* (Opinion No. 468), *supra* note 22, 34 F.P.C. at 185-189, 207-220, 239, new rates established, *Permian Basin Area Rate Proceeding* (Opinion No. 662), 50 F.P.C. 390 (1973), *modified on rehearing,* (Opinion No. 662-A), 50 F.P.C. 932 (1973); *Southern Louisiana Area Rate Proceeding* (Opinion No. 546), 40 F.P.C. 530, 544,

it was so commonplace and prominent in area ratemaking that the Commission itself acknowledged that "vintaging by contract date has become a hallmark of the area rate structure. . . ." [36] In the same breath, however, the Com-

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636-648 (1968), *modified on rehearing* (Opinion No. 546-A), 41 F.P.C. 301 (1969), aff'd *sub nom. Southern Louisiana Area Rate Cases, (Austral Oil Co.* v. *FPC)*, 428 F.2d 407 (5th Cir. 1970), *on rehearing*, 444 F.2d 125 (5th Cir. 1970), *cert. denied*, 400 U.S. 950, 91 S.Ct. 241, 27 L.Ed.2d 257 (1970), new rates established, *Southern Louisiana Area Rate Proceeding* (Opinion No. 598), 46 F.P.C. 86, 105, 134-139, 142-143 (1971), *clarified on rehearing* (Opinion No. 598-A), 46 F.P.C. 633 (1971), *aff'd sub nom. Placid Oil Co.* v. *FPC*, 483 F.2d 880 (5th Cir. 1973), *aff'd sub nom. Mobil Oil Corp.* v. *FPC, supra* note 1; *Hugoton-Anadarko Area Rate Proceeding* (Opinion No. 586), 44 F.P.C. 761, 772-776, 786-787 (1970), *aff'd sub nom. In re Hugoton-Anadarko Area Rate Case, (California* v. *FPC)*, 466 F.2d 974 (9th Cir. 1972); *Appalachian-Illinois Basin Area Rate Proceeding* (Opinion No. 411), 44 F.P.C. 1112, 1121-1125, 1130 (1970), *modified* (Opinion No. 411-A), 44 F.P.C. 1334 (1970), *rehearing denied* (Opinion No. 411-B), 44 F.P.C. 1487 (1970), *establishment of new area rates declined, Appalachian-Illinois Basin Area Rate Proceeding* (Opinion No. 639), 48 F.P.C. 1299 (1972), *aff'd sub nom. Shell Oil Co.* v. *FPC*, 491 F.2d 82 (5th Cir. 1974); *Texas Gulf Coast Area Rate Proceeding*, (Opinion No. 595), 45 F.P.C. 674, 705-709 (1971), *modified on rehearing* (Opinion 595-A), 46 F.P.C. 827 (1971), *vacated and remanded sub nom. Public Serv. Comm'n* v. *FPC*, 159 U.S.App.D.C. 172, 487 F.2d 1043 (1973), *vacated and remanded sub nom. Shell Oil Co.* v. *FPC*, 417 U.S. 964, 94 S.Ct. 3166, 41 L.Ed.2d 1136 (1974), *on remand sub nom. Public Serv. Comm'n* v. *FPC*, —— U.S.App. D.C. ——, 516 F.2d 746 (1975); *Other Southwest Area Rate Proceedings* (Opinion No. 607), 46 F.P.C. 900, 909, 913-919, 923-924 (1971), *modified on rehearing* (Opinion No. 607-A), 47 F.P.C. 99 (1971), *aff'd sub nom. In re Other Southwest Area Rate Cases (Shell Oil Co.* v. *FPC)*, 484 F.2d 469 (5th Cir. 1973), *cert. denied*, 417 U.S. 973, 94 S.Ct. 3180, 41 L.Ed. 2d 1144 (1974). See also *Rocky Mountain Area Rate Proceeding* (Opinion No. 658), 49 F.P.C. 924, 942-944, 947-948, 949-950 (1973), *rehearing denied*, 49 F.P.C. 1279 (1973).

[36] *Appalachian-Illinois Area Rate Proceeding* (Opinion No. 639), *supra* note 35, 48 F.P.C. at 1309.

mission declared that vintaging is "an anachronism which we should now move to eliminate," [37] and announced that thereafter, as an incentive to full exploration of the productive capability of gas fields in operation, "old" gas might be priced as "new" gas upon expiration of existing contracts of sale.[38] The orders presently under review undertake to carry that policy out to its full limit.

In Nos. 73-1647 and 73-1793, the orders authorize the three producer-applicants to incorporate the higher "new" rate in contracts executed after expiration of older contracts covering sales from the same sources of supply.[39] In No. 73-1794, the orders permit Mobil to substitute Texas Eastern for Shell as the immediate purchaser, at the "new" rate, of "old" gas taken from the same field from which Shell was supplied.[40] In each instance, flowing

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[37] *Id.*

[38] *Id.* at 1309-1310.

[39] The Commission approved the rate increases on the basis of the interpretations announced in Opinion No. 639, that "the new gas ceilings established under previous area rate opinions should apply to sales of natural gas made pursuant to 'new' contracts in those situations where deliveries of gas were previously certificated and dedicated to the interstate market under 'old' contracts which have expired by their own terms." *Continental Oil Co.*, —— F.P.C. ——, —— (1973) (order accepting rate filings) (J.App. 24).

[40] Mobil had sold gas to Shell, which in turn had gathered, processed and resold the gas to Texas Eastern. The orders in question authorized Mobil to abandon further sales to Shell under the expired Mobil-Shell contract and to sell the same gas directly to Texas Eastern at the "new" price. The service by Mobil appears to be merely a continuation of deliveries commenced during the "old"-rate era, and despite elimination of Shell's "middle man" status, Shell would continue to provide the same processing and delivery services as before. *Mobil Oil Corp.*, 49 F.P.C. 1009-1010 (1973) (order approving abandonment).

gas developed at cheaper costs can now be sold at the higher rate, without any effort whatever to find or dedicate new gas-well gas to the interstate community.

This, I repeat, is wholly in line with the Commission's declaration in Opinion No. 639 of the policy allowing newly executed contracts to be treated as "new" gas contracts under the area rate structure, even though such contracts serve merely to continue gas sales commenced during earlier periods to which the "old"-gas price ceiling for the area was applicable.[41] The ultimate consequence of permitting "new"-rate contracts to supplant existing "old"-rate contracts becomes apparent when it is recalled that eventually all time-limited "old" gas-sale contracts will run their course and new contracts at the "new" rate will inevitably follow. Vintaging will thus disappear step by step; as the Commission acknowledges, "[i]n time this [technique] will result in the elimination of a two-price system."[42]

As ground for this approach, the Commission has offered only a brief explanation:

> Vintaging operates to discourage development of the full productive capacity of acreage committed to the interstate market, for even though such developmental drilling is undertaken at current costs, gas production obtained thereby is priced at the *lower* of two rates, when it is the *higher* of the two that is Commission-designed to provide the incentive for development of additional gas supplies.[43]

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[41] *Appalachian-Illinois Basin Area Rate Proceeding* (Opinion No. 639), *supra* note 35, 48 F.P.C. at 1309-1310.

[42] *Id.* at 1310.

[43] *Id.* at 1309. Four months later, the Commission spoke again to the demise of the vintaging concept, echoing essentially the same theme:

> Whatever the merits of contract vintaging when adopted, we do not believe this concept responds to the present

> need for increased exploration and development. Exploration and development undertaken at current cost levels is retarded if the risk-taken knows that any gas found will be priced on the basis of historic, noncurrent costs. Similarly, the incentive factors applied in "new" gas ratemaking are totally lost as to undeveloped acreage committed under old contracts.
>
> Rates based on historic costs should apply to that gas brought to market at the historic cost levels relied upon in setting the rates. . . .

Rocky Mountain Area Rate Proceeding (Opinion No. 658), *supra* note 35, 49 F.P.C. at 943.

In the proceedings under review, the Commission did not offer any additional rationale; it simply accepted Opinion No. 639 as the controlling precedent. In the order under review in Nos. 73-1647 and 73-1793, the Commission ruled:

> In Opinion No. 639 we concluded that the new gas ceilings established under previous area rate opinions should apply to sales of natural gas made pursuant to "new" contracts in those situations where deliveries of gas were previously certificated and dedicated to the interstate market under "old" contracts which have expired by their own terms. That conclusion was based on our determination to interpret literally the vintaging provisions contained in area rate opinions.
>
> In the present cases each producer has entered into a new contract and his old contract has expired. Accordingly, under our interpretation of area rate opinions in Opinion No. 639, each of the subject increases to the new gas ceiling is acceptable.

Continental Oil Co., supra note 39, —— F.P.C. at ——, (J.App. 24). In the order denying rehearing of the order under review in No. 73-1794, the Commission declared that the allegations seeking rehearing

> appear to be primarily a collateral attack on [Opinion No. 639], which modifies our vintage pricing concept by allowing producers to collect "new gas rates" where an old contract expires by its own terms and a new contract is negotiated. . . . No further discussion of this issue is needed in this proceeding.

Mobil Oil Corp., supra note 43, 49 F.P.C. at 1412 (order denying rehearing).

That, in my view, is legally inadequate as a predicate for the Commission's action.[44] I submit that the orders in question lack sufficient supporting evidence [45] and fail to reflect the reasoned consideration due,[46] and accordingly are beyond the Commission's authority.[47]

Until the Commission forsook vintaging, it had functioned as the only process by which situations wherein exploratory and developmental ventures were likely—the "new" gas situations—were broadly differentiated, in terms of incentive components of a rate, from those wherein there was little or no such likelihood. I do not say that the Commission cannot under any conditions phase out or abandon price-vintaging as a regulatory mechanism; only recently we observed that "[w]ithin the limits imposed by the requirement of reasoned decision-making, the Commission is free to modify or even reverse its established policy." [48] I do say that when, as here, the Commission allows "old" gas to command the higher "new" gas price in the name of incentive, its action must be suitably justified.

There is obviously a sharp inherent difference between "old" and "new" gas in terms of the probability that a

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[44] It is settled, of course, that the "order[s] must be upheld, if at all, 'on the same basis articulated in the order[s] by the agency itself.'" *FPC* v. *Texaco, Inc., supra* note 12, 417 U.S. at 397, 94 S.Ct. at 2326, 41 L.Ed.2d at 156, quoting *Burlington Truck Lines* v. *United States*, 371 U.S. 156, 169, 83 S.Ct. 239, 246, 9 L.Ed.2d 207, 216 (1962). See also *SEC* v. *Chenery Corp.*, 332 U.S. 194, 196, 67 S.Ct. 1575, 1577, 91 L.Ed. 1995, 1999 (1947).

[45] Part II *infra*.

[46] Part III *infra*.

[47] See text *infra* at notes 123-124.

[48] *Consolidated Gas Supply Corp.* v. *FPC*, No. 74-1343 (D.C. Cir. Oct. 9, 1975), at 72 (footnotes omitted).

price increase indiscriminately applicable to all gas will stimulate either exploration or development.[49] For "new" gas the latter are a must; without a fresh gas find brought into production, the higher price is never realized. But for gas already flowing, no effort beyond the simple step of charging the higher price is required, and the incentive scheme achieves its objective only if the price increase attracts the activity needed to enlarge the supply of "new" gas. Since, to the extent that the scheme fails, the inevitable result is an excessive rate providing windfalls for producers, I believe it legally incumbent upon the Commission to find, on the basis of both evidence and logic, a reasonable probability that the scheme will succeed. I am unable to perceive either predicate in these cases.

II

Factual determinations by the Commission, I reiterate, must be supported by substantial evidence.[50] That requirement springs from the very legislation empowering the Commission to regulate interstate transactions in natural gas.[51] As we have observed in the past, "[i]t is highly significant that this substantial evidence test is a part of the actual language of the Natural Gas Act," [52] for "[t]his indicates that Congress was particularly concerned with the degree of certainty required in establishing factual predicates in rate-making." [53] I am unable to

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[49] I do not suggest that the lower rates may not under proper conditions include a noncost factor representing a share of the financial burden of exploration for and development of sources of "new" gas. See text *infra* at note 79.

[50] See cases cited *supra* note 7 and *infra* this Part II.

[51] Natural Gas Act § 19(b), 15 U.S.C. § 717r(b) (1970).

[52] *Mobil Oil Corp.* v. *FPC*, 157 U.S.App.D.C. 235, 254-255 n.68, 483 F.2d 1238, 1257-1258 n.68 (1973).

[53] *Id.*

discern any appreciable degree of evidentiary certainty underlying the orders contested here.

The one justifying consideration articulated by the Commission at all relevant to its action in these cases is the need to spur "development of the full productive capacity of acreage committed to the interstate market." [54] The one obstacle identified by the Commission is that only the "new" price for gas already flowing from that acreage will provide sufficient incentive to do so.[55] An elementary difficulty, however, is that the records before us are devoid of any evidence tending to show that allocation of the "new" price for what in reality is "old" gas is likely to achieve the Commission's stated objective.

In the *Permian Basin Area Rate Cases*,[56] the seminal authority for incentives in rate orders, the Court sustained the two-tiered pricing scheme there involved because the Commission had found, "*on the basis of substantial evidence*, that a two-price rate structure will both provide a useful incentive to exploration and prevent excessive producer profits." [57] The "new" gas price had been carefully constructed on data reflecting current costs of finding and developing new gas-well gas, and that price in turn was the stimulus which the Commission had sought.[58] "The inducement to be found in the 'new' gas price" was "of an inherent nature," [59] the Commission had said; "[t]he incentive" was "built into the two-price system;" [60]

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[54] See text *supra* at note 43.

[55] See text *supra* at note 43.

[56] (*Continental Oil Co.* v. *FPC*), *supra* note 1.

[57] 390 U.S. at 798, 88 S.Ct. at 1376, 20 L.Ed.2d at 353-354.

[58] See text *supra* at notes 25-34 and notes 25, 30 *supra*.

[59] *Permian Basin Area Rate Proceeding* (Opinion No. 468), *supra* note 22, 34 F.P.C. at 186.

[60] *Id.*

and what had emanated was "a price for the future related to current and future costs and payable only to producers who discover gas-well gas and dedicate their discoveries to the interstate market." [61] But now, as gas contracts expire, the Commission would obliterate the price variation predicated on vintaging, and with it the built-in incentive furnished by the fact that the higher price was available only as a reward for renewed exploratory and developmental effort.

Beyond cavil, extension of the "new" area rate to successor contracts covering still-flowing "old" gas is totally without evidence specifically underpinning the Commission's premise that the move presages fuller development of acreage producing beneath its potential. Neither the Commission nor any of the intervenors is able to point to any evidence of that type,[62] either in the proceeding leading to Opinion No. 639 or in the records before us.[63] The

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[61] *Id.*

[62] At oral argument we invited memoranda by the parties identifying and discussing the evidentiary bases, if any, for the orders now under review. I am unable to find in the submissions responsive to that invitation any reference to evidence bearing directly on the question whether allowance of the "new"-gas rate for "old" gas in replacement-contract situations, without more, is really calculated to bring about maximum development of existing fields and additional gas for the interstate community. That question is not answered affirmatively by evidence, in the proceeding generating Opinion No. 639, merely to the effect that price-vintaging has failed to achieve that goal, for it does not establish ipso facto a reasonable likelihood that the new pricing formula will succeed. Nor is the gap filled by testimony, in area rate proceedings antedating Opinion No. 639, which advocated abolition of all vintaging, for nothing in Opinion No. 639 indicates that the Commission accepted—or how it might have accepted—such testimony for that purpose. See notes 64, 90 *infra*.

[63] The findings to which the majority opinion refers relate only to the portion of Opinion No. 639 refusing to establish a

orders under review plainly proceed on the notion that Opinion No. 639's interpretation of vintaging orders—a nonevidentiary adjudication [64]—furnishes an ample predicate, and that no more is necessary.[65]

Surely, unlike the two-price feature comprising area-rate vintaging,[66] permission to charge the "new" rate for

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new third-vintage gas price in the Appalachian-Illinois Basin. See notes 64, 90 *infra*. Nowhere in Opinion No. 639 does the Commission undertake to elucidate a connection between its repricing policy and a beneficial effect on gas supply for the interstate market. My colleagues candidly acknowledge uncertainty that additional revenues from sales of flowing gas will lead to increased development or production, and for all we know the prospect may be forlorn.

Moreover, my colleagues' observation that the justness and reasonableness of preexisting area rates was determined in the respective proceedings leading to the orders setting those rates seems to me to be wide of the mark. Those rates were formulated on the basis of vintaging. See note 35 *supra* and accompanying text. My thesis is that rates which are just and reasonable when vintaged are not necessarily just and reasonable when vintaging is eliminated.

[64] The portion of Opinion No. 639 relevant to the instant cases emanated from a suggestion that a new third-vintage gas price be established in the Appalachian-Illinois Basin. The Commission denied that request. *Appalachian-Illinois Basin Area Rate Proceeding* (Opinion No. 639), *supra* note 35, 48 F.P.C. at 1306-1309. The Commission then, however, proceeded to address the two-price rate-vintaging aspect of the existing area rate order, and held that vintaging should be eliminated. *Id.* at 1309-1310. See also text *supra* at note 43. The mechanism by which the Commission accomplished this modification of rate design was its "interpretation" of the area-rate order vintaging provisions that when current contracts dedicating gas to the interstate market expire and new contracts are made, sales thereunder will be priced at the "new"-gas price ceiling. *Id.* at 1310. See also note 90 *infra*.

[65] Both orders under review accept Opinion No. 639 as an adequate foundation. See note 43 *supra*.

[66] See text *supra* at notes 22-35.

"old" gas does not readily suggest increased exploration and development as probable results.[67] When the higher price is obtainable only for gas that is truly "new," [68] an inducement to enlarge the supply may become fairly evident. The nexus between the price and the inducement may appear simply as a matter of ordinary human experience; as the authorized price for jurisdictional gas goes up, so may also the inducement to sell gas in the interstate market. Producers of natural gas are in business to make money, and a price high enough, if limited to gas really "new," is well calculated to attract efforts to locate undiscovered reserves, to develop virgin deposits and to put undedicated gas into interstate pipelines.

The same cannot be said nearly as confidently for allowance of the higher "new" price for gas from a field already known, producing and committed to interstate distribution. Under the plan projected by Opinion No. 639, the "new" price is not restricted to gas produced from new wells developed in that field; rather, all gas from the field would command the "new" price, including gas discovered, developed and dedicated long ago. Like the Fifth Circuit, the most I can say is that it is merely "conceivable" that the expectations of Opinion No. 639 will become a reality; [69] like my colleagues, I cannot say with any degree of assurance that it actually will.[70] In this milieu, there is, at least for me, a call for evidence resolving affirmatively the critical question whether the Commission's policy of pricing "old" gas at the "new" rate is promising enough as an incentive to survive the test of reasonableness.[71]

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[67] See text *supra* at note 49.

[68] See text *supra* at notes 26-27.

[69] See text *infra* at notes 84-90.

[70] See note 63 *supra*.

[71] See text *supra* at notes 10-11 and *infra* at notes 105-107.

I am mindful, of course, of the natural gas shortage now plaguing the Nation, and of the vigilant and serious consideration the Commission must give it in its regulatory activities.[72] In recent times, we have reviewed a number of Commission orders designed to instigate additional exploration and development by the natural gas industry,[73] and unfailingly have given prominence to the scarcity of gas and the need to provide incentives of that type.[74] But we have also been sensitive to our statutory responsibility [75] to make certain that there is substantial evidence in the record as a whole to sustain the particular incentive scheme under review.[76] And while we have "recog-

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[72] See, *e.g.*, *Mobil Oil Corp.* v. *FPC*, *supra*, note 1, 417 U.S. at 316-321, 94 S.Ct. at 2349-2352, 41 L.Ed.2d at 99-102; *FPC* v. *Louisiana Power & Light Co.*, 406 U.S. 621, 626, 92 S.Ct. 1827, 1831, 32 L.Ed.2d 369, 376-377 (1972); *Permian Basin Area Rate Cases (Continental Oil Co.* v. *FPC)*, *supra* note 1, 390 U.S. at 795-799, 88 S.Ct. at 1374-1377, 20 L.Ed.2d at 353-354; *Cities of Fulton* v. *FPC*, *supra* note 5, —— U.S.App.D.C. at ——, 512 F.2d at 950-951; *Moss* v. *FPC*, *supra* note 6, 161 U.S.App.D.C. at 5, 502 F.2d at 465.

[73] *E.g.*, *Cities of Fulton* v. *FPC*, *supra* note 5, —— U.S.App. D.C. at ——, 512 F.2d at 950-954; *Public Serv. Comm'n* v. *FPC*, *supra* note 35, —— U.S.App.D.C. at ——, 516 F.2d at 749; *Consumers Union of United States* v. *FPC*, 166 U.S. App.D.C. 276, 278-280, 510 F.2d 656, 658-660 (1974); *Macdonald* v. *FPC*, *supra* note 1, 164 U.S.App.D.C. at 255-259, 505 F.2d at 324-328.

[74] See cases cited *supra* note 73.

[75] See Natural Gas Act § 19(b), 15 U.S.C. § 717r(b) (1970).

[76] See, *e.g.*, cases cited *supra* note 73. We have noted that "[u]nder the shadow of the nationwide shortage of natural gas, the incentive device has been seized upon increasingly by the [Commission] and paraded before the courts in a number of guises, perhaps on the assumption that the courts would be inclined to reject them all," *Cities of Fulton* v. *FPC*, *supra* note 5, —— U.S.App.D.C. at ——, 512 F.2d at 950-951

nize[d] that agency expertise is to be accorded deference," [17] we have taken pains to deny that this "principle[] can substitute for the adequate evidentiary basis upon which the Commission's finding[s] must rest." [18] In the case at bar, there simply is no evidence as to whether the questioned orders will, as a matter of reasonable prospect, lead to an alleviation of the shortage.[19]

(footnote omitted), and we have listed a number of such guises. *Id.* n.19. We have remained faithful to our obligation in each case to examine the record to determine whether we are faced "with a change in direction put in effect for a navigational objective, or the confusion of an agency that is rudderless and adrift." *Public Serv. Comm'n* v. *FPC*, *supra* note 1, 167 U.S.App.D.C. at 115, 511 F.2d at 353.

[17] *Memphis Light, Gas & Water Div.* v. *FPC*, *supra* note 1, 164 U.S.App.D.C. at 165, 504 F.2d at 234.

[18] *Id.* Not even the spectre of an undesirable situation, "unsupported by any evidence that it could occur in fact, justifies" a regulatory procedure. *Memphis Light, Gas and Water Div.* v. *FPC*, *supra* note 1, 164 U.S.App.D.C. at 164, 504 F.2d at 233. What are required are "not mere fears for the future but facts and findings, a statement of reasons that is supported by concrete inferences from substantial evidence, and is not to be snatched from the air on a purely hypothetical 'worse case' analysis. . . ." *Id.* at 165, 504 F.2d at 234.

[19] As was held in *Mobil Oil Corp.* v. *FPC*, *supra* note 1, the Commission may under proper conditions incorporate into the "old"-gas rate a noncost factor as an incentive to expand production. "As between placing the burden of that expansion on new or second vintage gas alone or spreading it over both old and new gas, [the Commission may] mudge [] the latter more equitable and more likely to lead to the immediately increased capital necessary in the face of a crisis;" in other words, it may "place the burden of those payments on all users rather than on those alone who purchased gas in the future." 417 U.S. at 320, 94 S.Ct. at 2352, 41 L.Ed.2d at 102. It should be noted, however, that there the Commission compiled a massive evidentiary record, a part of which "focused on the gas shortage, projected levels of demand, and esti-

I do not gainsay the need to accord the Commission wide latitude in its efforts to find ways and means of combating the gas deficiency.[80] A "broad discretion . . . has been entrusted to the Commission," we have said, " 'to devise methods of [natural gas] regulation capable of equitably reconciling diverse and conflicting interests,' and [the Commission's] discretion must be given particular respect 'in this time of acute energy shortage.' "[81] But we have also said that "the purposes of the Natural Gas Act, including those of protecting consumers from prices which are forced above a just and reasonable level by the market power of natural gas suppliers, impose limits on this discretion."[82] As the Supreme Court has declared, "[t]he Commission [is] bound to exercise its discretion within the limits of the standards expressed by the Act; and 'for the courts to determine whether the agency *has* done so, it must 'disclose the basis of its order' and 'give clear in-

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mates of new supply needed to alleviate the problem," and another part of which bore "upon rate levels needed to induce additional supply, the potential industry consequences of any new order, and new cost trends based on [new] data. . . ." *Id.* at 296, 94 S.Ct. at 2340, 41 L.Ed.2d at 88. In contrast, there is no evidentiary foundation for either of the orders before us or for the order accompanying Order No. 639, upon which they are based. See notes 62-63 *supra*.

[80] See *Mobil Oil Corp.* v. *FPC*, *supra* note 1, 417 U.S. at 331, 94 S.Ct. at 2356-2357, 41 L.Ed.2d at 107-108; *Cities of Fulton* v. *FPC*, *supra* note 5, —— U.S.App.D.C. at ——, 512 F.2d at 951; *Macdonald* v. *FPC*, *supra* note 1, 164 U.S.App. D.C. at 250, 505 F.2d at 357.

[81] *Macdonald* v. *FPC*, *supra* note 1, 164 U.S.App.D.C. at 250, 505 F.2d at 357, quoting *Mobil Oil Corp.* v. *FPC*, *supra* note 1, 417 U.S. at 331, 94 S.Ct. at 2356-2357, 41 L.Ed.2d at 107-108. See also *Cities of Fulton* v. *FPC*, *supra* note 5, —— U.S.App.D.C. at ——, 512 F.2d at 951.

[82] *Macdonald* v. *FPC*, *supra* note 1, 164 U.S.App.D.C. at 250, 505 F.2d at 357.

dication that it has exercised the discretion with which Congress has empowered it.'" [83] In my view, the basis thus far revealed by the Commission is inadequate to bring its action within the confines of its statutory authority.

The conclusion my colleagues reach in these cases is not sustained by the Fifth Circuit's decision in *Shell Oil Company* v. *Federal Power Commission*,[84] upon which they rely; indeed, it is antithetical to the holding in *Shell*. There the court reviewed, not concrete applications of Opinion No. 639 as here, but the opinion—the interpretative rule—itself. Thus for good reason the court deemed the appropriate inquiry to be simply whether that opinion's interpretation of the Commission's vintaging regulations, a matter commanding judicial deference,[85] was

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[83] "The Commission [is] bound to exercise its discretion within the limits of the standards expressed by the Act; and 'for the courts to determine whether the agency *has* done so, it must 'disclose the basis of its order' and 'give clear indication that it has exercised the discretion with which Congress has empowered it.'" *FPC* v. *Texaco, Inc., supra* note 12, 417 U.S. at 396, 94 S.Ct. at 2325, 41 L.Ed.2d at 155, quoting *Burlington Truck Lines* v. *United States, supra note* 44, 371 U.S. at 167-168, 83 S.Ct. 239, 245-246, 9 L.Ed.2d 207, 215-216, in turn quoting *Phelps Dodge Corp.* v. *NLRB*, 313 U.S. 177, 197, 61 S.Ct. 845, 853-854, 85 L.Ed. 1271, 1284-1285 (1941) (emphasis in original).

[84] *Supra* note 35.

[85] *Udall* v. *Tallman*, 380 U.S. 1, 16-17, 85 S.Ct. 792, 801-802, 13 L.Ed.2d 616, 625-626 (1965); *Bowles* v. *Seminole Rock Co.*, 325 U.S. 410, 413-414, 65 S.Ct. 1215, 1217, 89 L.Ed. 1700, 1702-1703 (1945); *Gulf Oil Corp.* v. *Hickel*, 140 U.S.App.D.C. 368, 372-373, 435 F.2d 440, 444-445 (1970); *Udall* v. *Oelschlaeger*, 129 U.S.App.D.C. 13, 15, 389 F.2d 974, 976 (1968), *cert. denied*, 392 U.S. 909, 88 S.Ct. 2056, 20 L.Ed.2d 1367 (1968).

"reasonable and consistent with the regulation[s]." [86] While recognizing the possibility that the interpretation Opinion No. 639 yielded may not lead to a larger gas supply,[87] the court noted that "[i]t is also conceivable . . . that a departure from vintaging will serve to increase

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[86] *Shell Oil Co.* v. *FPC*, *supra* note 35, 491 F.2d at 88. Compare *Public Serv. Comm'n* v. *FPC*, *supra* note 35, —— U.S. App.D.C. at ——, 516 F.2d at 750; *Moss* v. *FPC*, *supra* note 6, 164 U.S.App.D.C. at 8, 502 F.2d at 468; *Public Serv. Comm'n* v. *FPC*, 151 U.S.App.D.C. 307, 317, 467 F.2d 361, 371 (1972).

[87] The court summarized the argument against the interpretative rule thusly:

> With "new" and flowing gas at the same price level, the producers will have no incentive to find more gas because they can reap windfall profits by selling cheap flowing gas at the higher rate formerly reserved for "new" gas. If [the Commission] required the producers to show higher costs or new production to justify the higher rate, then [the Commission] would be acting rationally. But it is irrational only to raise gas rates with no *quid pro quo* required. The producers will not find increased production to be in their best interest, and, as [New York Public Service Commission] puts it, they will "take the money and run."

Shell Oil Co. v. *FPC*, *supra* note 6, 491 F.2d at 89. The court then acknowledged that:

> [New York Public Service Commission's] pessimism is understandable and may, in time, prove justified. It is true that producers who sign new contracts at the current area rates will find their "old gas" rate boosted by an increment greater than their cost increases. And it is possible, as [New York Public Service Commission] forecasts, that producers will reap the new high rates for their flowing gas without engaging in further drilling.

Id.

production," [88] and on that basis concluded that the Commission's "interpretation of its regulations' vintaging provision is rational, reasonable, and therefore fully permissible." [89] But the court was careful to state that

> [a] caveat is appropriate at this point. In regard to vintaging, today we are approving [the Commission's] interpretation of certain regulations. We do not reach the question of whether [the Commission] may altogether discontinue the use of vintaging. Rather in each future rate order the Commission must continue to produce substantial evidence to support each essential element of the proposed rate structure. . . . Certainly the absence or presence of vintaging must be regarded as an essential element.[90]

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[88] *Id.* The Court explained:

> If a producer has signed a contract before the division date, all the gas he produces during the contract's life will receive the low "old gas" price. Even if he drills new wells at current costs, the "new" gas he discovers and produces will be priced as "old" gas, on the basis of historical costs computed in a year long since goneby. Since costs seem to rise inexorably with the passage of time, new drilling will become less attractive as the contract ages. For example, we think it quite likely that a producer operating under a 1964 contract may have little incentive to find expensive 1974 gas only to sell it at bargain 1964 rates. But if he can raise his prices to a uniform rate for both "new" and "old" gas when the old contract expires and a new one is signed, he might be more inclined to drill new wells.

Id.

[89] *Id.*

[90] *Id.* at 89-90. It had been argued that Opinion No. 639's "vintaging statement is a basic modification of [Commission] regulations, and not the permissible interpretation it is advertised to be," and that "[t]herefore the vintaging statement should have been preceded by notice and a hearing and supported by record evidence, in accordance with the rulemaking prerequisites set out in Section 4 of the Administra-

In the cases at bar, we are summoned to examine the interpretative rule, not in the sterile context of a rule-making review, but in operation in rate orders addressing concrete situations. The orders are clearly of the type which *Shell* referred to in its call for substantial evidence to support the absence of a vintaging component from their rate structures.[91] I agree with the Fifth Circuit that that absence is an essential element of the orders, and as such depended on an ample evidentiary foundation for survival.[92] The majority position here, in treating supporting evidence as an unnecessary commodity, not only disregards *Shell's* specific ruling on the point but, more

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tive Procedure Act." *Id.* at 87 (footnoting 5 U.S.C. § 553 [1970]). The court disagreed because it "believe[d] the vintaging statement is a permissible interpretation, not a basic modification of rate-setting regulations," and "[w]hether we characterize the statement as an interpretation or an interpretative rule, notice, a hearing and a record were not required." *Id.* (citations and footnote omitted). See also Administrative Procedure Act, § 4(a), 5 U.S.C. § 553(b) (1970).

[91] For this reason, I agree with my colleagues that the decision in *Shell* erects no barrier to our consideration of the questions whether the Commission's conclusions are supported by substantial evidence and are products of "reasoned consideration." Compare *Public Service Comm'n* v. *FPC, supra* note 1, 167 U.S.App.D.C. at 103, 511 F.2d at 341.

[92] See cases cited *supra* note 7 and this Part II. My colleagues accept the orders under review as permissible applications of Opinion No. 639, and the latter in turn as a reasonable interpretation of the vintaging provisions of the applicable area-rate orders. I suggest that the inquiry should not stop at this point. The ultimate question is whether application of the "new"-gas price for what is actually "old" gas results in just and reasonable charges to the consuming public; and the answer depends upon factual conclusions fairly drawn from relevant evidence and reasoned consideration by the Commission of the pertinent factors. Until the Commission engages in these processes, the holding on interpretation obscures the real issue. See note 63 *supra*.

fundamentally, also ignores the Supreme Court's mandate on that score.[93]

III

Beyond advertence to the need for supporting evidence, this court has consistently enforced the Supreme Court's mandate [94] that the Commission give "reasoned consideration" to each and every factor pertinent to its decision.[95] As we have had occasion to state, "[r]espect for the broad discretion of the [Commission] and appreciation of its difficult regulatory task impel us to uphold the Commission when it perceives the central problems, diligently seeks information to assist it in resolving those issues, and exercises its judgment in the light of that information." [96] But as we have also made clear, "in applying the 'substantial evidence test . . . reasoned conclusions are the hallmark of regularity,'" [97] and "the reviewing court's duty to 'assure fidelity to the functions assigned to the regulatory agency by Congress' requires that it hold the agency to its duty to give reasoned consideration to the

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[93] See note 1 *supra*.

[94] See note 1 *supra*.

[95] *Public Serv. Comm'n* v. *FPC*, *supra* note 1, 167 U.S.App. D.C. at 107, 511 F.2d at 345; *Macdonald* v. *FPC*, *supra* note 1, 164 U.S.App.D.C. at 256-258, 505 F.2d at 363-365; *Texas Gulf Coast Area Rate Cases (Public Serv. Comm'n* v. *FPC)*, *supra* note 35, 159 U.S.App.D.C. at 208, 487 F.2d at 1049; *City of Chicago* v. *FPC*, 147 U.S.App.D.C. 312, 325, 458 F.2d 731, 744 (1971), *cert. denied*, 405 U.S. 1074, 95 S.Ct. 1495, 35 L.Ed. 2d 808 (1972); *City of Chicago* v. *FPC*, 128 U.S.App.D.C. 107, 115, 385 F.2d 629, 637 (1967), *cert. denied*, 390 U.S. 945, 88 S.Ct. 1028, 19 L.Ed.2d 1133 (1968).

[96] *Public Serv. Comm'n* v. *FPC*, *supra* note 1, 167 U.S.App. D.C. at 112, 511 F.2d at 354 (footnote omitted).

[97] *Id.* at 107, 511 F.2d at 345, quoting *City of Chicago* v. *FPC*, *supra* note 95, 147 U.S.App.D.C. 325, 458 F.2d at 744.

facts and issues material to its determinations." [98] I think the Commission should be bound to that duty here.

The reasoned-consideration requirement obtains with respect to incentive features of the Commission's rate orders as much as it does to any other.[99] To be sure, "an inability to 'determine the precise amount of additional gas supply that would be found and dedicated to interstate sales' as a result of the incentive formula" is not necessarily fatal to the order.[100] And certainly "[c]ourts 'cannot fairly demand the perfect at the expense of the achievable' and ought not insist on findings which are 'unrealistically and unnecessarily refined.' " [101] But "problems which preclude precise quantification do not excuse the Commission's abdication of its duty to indicate 'fully and carefully the methods by which, and the purposes for which, it has chosen to act, as well as the consequences of its orders for the character and future development of the industry.' " [102] That, I say, the Commission has not done here.[103]

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[98] *Public Serv. Comm'n* v. *FPC*, *supra* note 1, 167 U.S. App.D.C. at 112, 511 F.2d at 354.

[99] See cases cited *infra* note 104.

[100] *Public Serv. Comm'n* v. *FPC*, *supra* note 1, 167 U.S. App.D.C. at 118, 511 F.2d at 346, quoting *Mobil Oil Corp.* v. *FPC*, *supra* note 1, 417 U.S. at 318, 94 S.Ct. at 2350, 41 L.Ed.2d at 100. See also *Public Serv. Comm'n* v. *FPC*, *supra* note 35, —— U.S.App.D.C. at ——, 516 F.2d at 749.

[101] *Public Serv. Comm'n* v. *FPC*, *supra* note 1, 167 U.S.App. D.C. at 118, 511 F.2d at 346, quoting *Texas Gulf Coast Area Rate Cases (Public Serv. Comm'n* v. *FPC)*, *supra* note 35, 159 U.S.App.D.C. at 196, 487 F.2d at 1067 (separate opinion of Leventhal, J.) (footnote omitted).

[102] *Public Serv. Comm'n* v. *FPC*, *supra* note 1, 167 U.S. App.D.C. at 118, 511 F.2d at 346, quoting *Permian Basin Area Rate Cases (Continental Oil Co.* v. *FPC)*, *supra* note 1, 390 U.S. at 792, 88 S.Ct. at 1373, 20 L.Ed.2d at 350.

[103] The Commission's treatment leaves a number of unanswered questions in its wake. What amount of added revenue

More specifically, the Commission has not shown that it gave " 'reasoned consideration' to the shaping of its order[s] in an effort to protect consumers from paying substantially more than necessary to bring forth the needed supplies." [104] "The purpose of the Natural Gas Act," we all know, "was to underwrite just and reasonable rates to the consumers of natural gas;" [105] its "primary aim . . . was to protect consumers against exploitation at the hands of natural gas companies." [106] In har-

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is needed to induce development of existing gas fields to full capacity? Is that amount more or less than the added revenue that will be yielded by allowing "old" gas to be sold at the "new" price? How much of the added revenue is likely to be devoted to developmental effort? What is the likelihood that additional gas supplies thus made available will reach the interstate market? What increase in cost to consumers expectably will result from the challenged orders? Mention of these questions is not, of course, an attempt to furnish a complete list. The point is that the Commission has not tried to answer any of them, on the basis of evidence or otherwise, and no one can be certain that the Commission " 'has given reasoned consideration' and 'appropriate protection' to the public interest in not paying prices for gas substantially in excess of those needed to induce production of an adequate gas supply." *Macdonald* v. *FPC, supra* note 1, 134 U.S.App. D.C. at 256, 505 F.2d at 363.

[104] *Cities of Fulton* v. *FPC, supra* note 5, —— U.S.App. D.C. at ——, 512 F.2d at 951. See also *Macdonald* v. *FPC, supra* note 1, 161 U.S.App.D.C. at 256, 505 F.2d at 363; *City of Chicago* v. *FPC, supra* note 95, 147 U.S.App.D.C. at 332, 458 F.2d at 751.

[105] *Atlantic Ref. Co.* v. *Public Serv. Comm'n, supra* note 17, 360 U.S. at 388, 79 S.Ct. at 1253, 3 L.Ed.2d at 1319.

[106] *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591, 610, 64 S. Ct. 281, 291, 88 L.Ed. 333, 349 (1944). Only recently the Supreme Court pointed out that:

> It is abundantly clear from the history of the Act and from the events that prompted its adoption that Congress considered that the natural gas industry was heavily

mony with that goal, "[t]he Act was so framed as to afford consumers a complete, permanent and effective bond of protection from excessive rates and charges." [107] On the administrative records in these cases as they now stand, we cannot discharge the responsibility of a reviewing court to determine whether the orders in question can rationally be expected to "provide appropriate protection to the relevant public interests, both existing and foreseeable." [108]

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concentrated and that monopolistic forces were distorting the market price for natural gas.

FPC v. *Texaco, Inc.*, *supra* note 12, 417 U.S. at 397-398, 94 S.Ct. at 2326, 41 L.Ed.2d at 156. The "only justification for giving the Commission the duty to regulate prices was the determination by Congress that the producers have a supply that is so restricted in relation to demand that they have the economic power to bargain for prices that will be injurious to the public." *United Gas Improvement Co.* v. *FPC*, 290 F. 2d 133, 135 (5th Cir.), *cert. denied*, 368 U.S. 823, 84 S.Ct. 41, 7 L.Ed.2d 27 (1961). See also *Macdonald* v. *FPC*, *supra* note 1, 164 U.S.App.D.C. at 257, 505 F.2d at 364.

[107] *Atlantic Ref. Co.* v. *Public Serv. Comm'n*, *supra* note 17, 360 U.S. at 388, 79 S.Ct. at 1253, 3 L.Ed.2d at 1319.

[108] "The Commission may not exceed its authority under the [Natural Gas] Act; its orders are subject to judicial review; and reviewing courts must determine whether Commission orders, issued pursuant to indirect regulation, are supported by substantial evidence and whether it is rational to expect them 'to maintain financial integrity, attract necessary capital, and fairly compensate investors for the risk they have assumed, and yet provide appropriate protection to the relevant public interest, both existing and foreseeable.' " *FPC* v. *Texaco, Inc.*, *supra* note 12, 417 U.S. at 393, 94 S.Ct. at 2324, 41 L.Ed.2d at 154, quoting *Permian Basin Area Rate Cases, (Continental Oil Co.* v. *FPC)*, *supra* note 1, 390 U.S. at 792, 88 S.Ct. at 1362-1363, 20 L.Ed.2d at 350. See also *Mobil Oil Corp.* v. *FPC*, *supra* note 1, 417 U.S. at 309, 94 S. Ct. at 2346, 41 L.Ed.2d at 96.

The challenged orders confer upon the producers the privilege of charging the higher "new" rate for gas from old wells brought to maturity during an era when the expense of exploration and development was much lower than it is today. The Commission's sole justification for this boon is the asserted need for an incentive to development of acreage in production to its maximum potential.[109] In no wise, however, do these orders provide any assurance that the new revenues thus generated will be devoted to that end. Had the orders conditioned receipt of the additional revenues on expenditures calculated to enlarge the productive capability of existing fields, the problem under discussion would hardly have arisen.[110] Nonetheless, the Commission, without any explanation whatsoever, has not imposed any such limitation upon its grant.

This is not the first time we have encountered this type of difficulty in the Commission's rate-increase orders. In *Macdonald* v. *Federal Power Commission*,[111] an independent producer's sales were approved at rates far above those established by the applicable area rate order, and the Commission sought to justify the rate raise by the producer's commitment to invest funds in further gas exploration and production. It appeared, however, that the additional revenues would greatly exceed the amount of the commitment, and in substantial part might be directed toward finds of gas or oil that would never reach the interstate market. We were "troubled by the Commission's failure to require [the producer] to invest in exploration for gas to be dedicated to the interstate market all of its . . . revenues in excess of those it would

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[109] See text *supra* at note 43.

[110] See note 116, *infra*.

[111] *Supra* note 1.

have obtained at the area rate." [112] We expressed our feeling that "[a] requirement that all the excess revenues be employed to ease the interstate gas shortage would have given symmetry to the purpose of the grant of relief and [the producer's] *quid pro quo* to obtain the relief." [113] We pointed out that "[t]he symmetry would have been perfected had the Commission given preemptive rights on the gas obtained from the exploration to [the pipeline] whose rate-paying consumers effectively funded new drilling." [114] It was unnecessary to consider whether this deficiency demanded redress since for other reasons a remand to the Commission was required.[115]

Here, even more than in *Macdonald*, there is a lack of assurance that the producers' added revenues will ever mean added gas supplies for the interstate community.[116]

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[112] 164 U.S.App.D.C. at 258 n.37, 505 F.2d at 565 n.37.

[113] *Id.*

[114] *Id.*

[115] *Id.* at 258, 505 F.2d at 565.

[116] Compare *Mobil Oil Corp.* v. *FPC*, *supra* note 1, where the Commission's order advanced incentives in the form of price escalations and refund-workoff credits contingent upon new dedications of gas to the interstate market, 417 U.S. at 298-300, 94 S.Ct. at 2340-2341, 41 L.Ed.2d at 89-90—programs on which the consuming public could not possibly lose. The Supreme Court approved. "[I]t was well within Commission discretion and expertise," the Court said, "to conclude that the refund workoff credits and contingent escalations could provide opportunity for increased prices that would help in generating capital funds and in meeting rising costs, while assuring that such increases would not be levied upon consumers unless accompanied by increased supplies of gas." *Id.* at 317-318, 94 S.Ct. at 2350, 41 L.Ed.2d at 100. And see the order reviewed in *Permian Basin Area Rate Cases* (*Continental Oil Co.* v. *FPC*), *supra* note 1, discussed in text *supra* at notes 25-34.

[Continued]

For there is no commitment of any sort by the producers, nor any requirement whatever by the Commission; there is, in other words, not so much as an understanding that any of the new funds will be invested in new wells in existing fields, or that any "new" gas therefrom will be directed to the interstate market. There is, moreover, no record evidence indicating a probability that attainment of those goals will automatically follow.[117] I believe that here there should be "a much tighter fit between [the

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[116] [Continued]

Compare also *Cities of Fulton* v. *FPC*, *supra* note 5, where the Commission conditioned approval of a gas sale, at applicable area rates in lieu of rates based on cost of service, upon expenditure of the excess of the new rates over the old rates in the development of new gas reserves, that amount to be spent over and above amounts already projected for exploration and development. The Commission also required refunds at a specified rate for each unit of gas by which the producers' effort fell short of the estimated yield of new gas. —— U.S.App.D.C. at ——, 512 F.2d at 949. We sustained the Commission's action. —— U.S.App.D.C. at ——, 512 F.2d at 951-956.

And see *Permian Basin Area Rate Cases* (*Continental Oil Co.* v. *FPC*), *supra* note 1, where the area rate order provided in part that the higher maximum rate would be applied retroactively to a period antedating the order. The Court observed that "[i]t is difficult to see how the higher rate could reasonably have been expected to encourage, retrospectively, exploration and production that had already occurred," with the result that "[t]here is thus force in [the] contention that this arrangement is not fully consistent with the logic of the two-price system." 390 U.S. at 798, 88 S.Ct. at 1376, 20 L.Ed.2d at 354 (footnote omitted). The Court upheld the provision because the Commission evidently believed that it was responsible for producer expectations of higher prices for initial filings, and a price reduction with accompanying refunds might have diminished confidence in interstate prices and thereby threatened the interstate supply. *Id.* at 798-799, 88 S.Ct. at 1376-1377, 20 L.Ed.2d at 354.

[117] See text *supra* at notes 57-61.

producers'] *quid pro quo* and the purposes for which the Commission acted," [118] and that the Commission should be required to provide it.[119]

IV

True it is that "[a] presumption of validity . . . attaches to each exercise of the Commission's expertise," and that "those who would overturn the Commission's judgment undertake 'the heavy burden of making a convincing showing that it is invalid because it is unjust and unreasonable in its consequences.' " [120] In my view, however, petitioners have demonstrated glaring deficiencies in the challenged orders which may well indulge them precisely that effect. In vital aspects they lack substantial supporting evidence in the administrative records [121] and reasoned consideration in the Commission's adjudicative exercises,[122]

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[118] *Cities of Fulton* v. *FPC*, *supra* note 5, —— U.S.App.D.C. at ——, 512 F.2d at 952.

[119] Compare *Transcontinental Gas Pipe Line Corp.* v. *FPC*, 160 U.S.App.D.C. 1, 5, 488 F.2d 1325, 1329 (1973); *cert. denied*, 417 U.S. 921, 94 S.Ct. 2629, 41 L.Ed.2d 226 (1974); *Michigan Consolidated Gas Co.* v. *FPC*, 108 U.S.App.D.C. 409, 431, 283 F.2d 204, 226, *cert. denied*, 364 U.S. 913, 81 S.Ct. 276, 5 L.Ed.2d 227 (1960). Since the stated purpose of eliminating vintaging was to encourage maximum development of committed acreage, see text *supra* at note 43, it seems clear that the Commission might have attained that goal simply by substituting vintaging by date of commencement of well-drilling in place of vintaging by contract date. See *Rocky Mountain Area Rate Proceeding* (Opinion No. 658), *supra* note 35, 49 F.P.C. at 942-943.

[120] *Mobil Oil Corp.* v. *FPC*, *supra* note 1, 417 U.S. at 307, 94 S.Ct. at 2345, 41 L.Ed.2d at 94, quoting *Permian Basin Area Rate Cases* (*Continental Oil Co.* v. *FPC*), *supra* note 1, 390 U.S. at 767, 88 S.Ct. at 1360, 20 L.Ed.2d at 336, in turn quoting *FPC* v. *Hope Natural Gas Co.*, 320 U.S. 591, 602, 64 S.Ct. 287-288, 88 L.Ed. 344-345 (1944).

[121] See Part II *supra*.

[122] See Part III *supra*.

each contributing to a potentially unlawful result. That result is an excessive rate for "old" gas from fields already in production, made possible by a complete lack of assurance, evidentiary or otherwise, that the excess of the "new"-gas rate over the "old"-gas rate will be channeled into a quest for additional gas supplies. Exorbitant rates are unjust and unreasonable rates,[123] beyond the authority of the Commission to prescribe.[124]

The Commission is "obligated at each step of its regulatory process to assess the requirements of the broad public interests entrusted to its protection by Congress." [125] This the Commission has not done, and I am unable to join in affirmance of the orders under review as they now stand. I would remand these cases to the Commission for further investigation of the critical issues which have not as yet been adequately addressed.

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[123] See text *supra* at notes 10, 105-107.

[124] See text *supra* at note 11.

[125] *Permian Basin Area Rate Cases* (*Continental Oil Co.* v. *FPC*), *supra* note 1, 390 U.S. at 791, 88 S.Ct. at 1372-1373, 20 L.Ed.2d at 350.

Appendix B

UNITED STATES OF AMERICA
FEDERAL POWER COMMISSION

AREA RATES

Before Commissioners: John N. Nassikas, Chairman; Albert B. Brooke, Jr., and Rush Moody, Jr.

Continental Oil Company, *et al.* [1]	FPC Gas Rate Schedule No. 3, *et al.*

ORDER ACCEPTING RATE FILINGS
AND
PERMITTING INTERVENTION
(Issued April 27, 1973)

The producers listed in the Appendix have filed proposed increased rates to the applicable area new gas ceiling based on the vintaging concepts set forth by the Commission in its Opinion No. 639 issued December 12, 1972.[2]

Associated Gas Distributors (AGD) has filed a petition to intervene and the Public Service Commission of the State of New York (PSCNY) has filed a notice of intervention in these proceedings. PSCNY in its notice states that it has sought judicial review of Opinion No. 639,[3] and as a result would be prepared to accept Commission orders suspending the increases for one day and providing that the collection of the increased rates subsequent thereto will be subject to refund with interest at 7% per annum in the event Opinion No. 639, insofar as it purports to authorize such increases, is reversed, remanded, or otherwise set aside upon review. To the extent producers are not prepared to accept such conditions, then

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[1] The other producers and rate schedules involved here are listed in the Appendix.

[2] Rehearing of that opinion was denied by order issued February 8, 1973.

[3] PSCNY *v. F.P.C.* (CADC No. 73, 1174

PSCNY requests that their increases be suspended for the full five month statutory period and set for prompt hearing.

In Opinion No. 639 we concluded that the new gas ceilings established under previous area rate opinions should apply to sales of natural gas made pursuant to "new" contracts in those situations where deliveries of gas were previously certificated and dedicated to the interstate market under "old" contracts which have expired by their own terms. That conclusion was based on our determination to interpret literally the vintaging provisions contained in area rate opinions.[4]

In the present cases each producer has entered into a new contract and his old contract has expired. Accordingly, under our interpretation of area rate opinions in Opinion No. 639, each of the subject increases to the new gas ceiling is acceptable. In these circumstances, there is no need for a hearing inasmuch as no factual issues are involved. Nor is there any justification for suspending the proposed rates, as PSCNY suggests, either because it disagrees with our interpretation of area rate opinions or because it has sought judicial review of Opinion No. 639. Such action would be contrary to the conclusions reached by us in Opinion No. 639.

We shall grant AGD's petition to intervene. No action is necessary in connection with PSCNY's notice of intervention inasmuch as under Section 1.8 of the Commission's Rules a State Commission, as a matter of right, may intervene in a proceeding by filing a notice.

The Commission orders:

(A) The proposed increased rates set forth in the Appendix are accepted as of the effective dates provided therein.

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[4] In our order denying rehearing we rejected PSCNY's contention that our interpretation was illegal and unwise.

(B) AGD is permitted to intervene in the above-entitled proceedings, subject to the rules and regulations of the Commission: *Provided, however,* that its participation shall be limited to matters affecting asserted rights and interests specifically set forth in its petition for leave to intervene: And, *provided, further,* that the admission of AGD in the manner provided shall not be construed as recognition by the Commission that AGD might be aggrieved because of any order or orders entered in these proceedings.

(C) The rate increases granted herein have been reviewed in the light of and are consistent with the Economic Stabilization Act of 1970 as amended, Executive Order 11695, and the Rules and Regulations issued thereunder.

By the Commission.

(S E A L)

Kenneth F. Plumb,
Secretary.

UNITED STATES OF AMERICA
FEDERAL POWER COMMISSION

Abandonment

Before Commissioners: John N. Nassikas, Chairman;
Albert B. Brooke, Jr., Rush Moody, Jr.,
and William L. Springer.

Mobil Oil Corporation (Operator),) Docket No. CI73-450
et al.

ORDER DENYING APPLICATION FOR REHEARING

(Issued June 21, 1973)

On May 16, 1973, the Associated Gas Distributors (AGD) filed in Docket No. CI73-450 an application pursuant to Section 19(a) of the Natural Gas Act for rehearing of our order of April 16, 1973, in said docket, which allowed Mobil Oil Corporation (Operator), *et al.* (Mobil), to abandon a sale of natural gas to Shell Oil Company (Shell) from the Provident City Field, Lavaca County, Texas. In a related

action on the same day in Docket No. CI73-451, Mobil was issued a temporary certificate authorizing sales of natural gas to Texas Eastern Transmission Corporation (Texas Eastern) from the same acreage.

AGD contends that Mobil's abandonment is not required by the public convenience and necessity and submits that the net result of Mobil's proposals is to increase the price of gas delivered to Texas Eastern from 19.0 cents per Mcf to 24.0 cents per Mcf.[1] AGD also asserts that it was inappropriate to treat the two applications separately and that the two applications by Mobil were no more than efforts to avoid the rate design adopted for the Texas Gulf Coast Area.[2] AGD further alleges that the record contains no supporting evidence for abandonment or for price relief.

AGD's allegations appear to be primarily a collateral attack on our order issued in Docket No. R-371, which modifies our vintage pricing concept by allowing producers to collect "new gas rates" where an old contract expires by its own terms and a new contract is negotiated.[3] AGD was a party to that proceeding where the issue of the appropriateness of our vintage modification was considered and decided. No further discussion of this issue is needed in this proceeding. In support of the new arrangement the record in this case clearly indicates that:

(1) Mobil's contract with Shell has terminated;

(2) The ultimate pipeline purchaser of the subject gas will remain the same;

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[1]Shell sold the gas which it purchased from Mobil to Texas Eastern.

[2]Commission Opinion No. 595, *Area Rate Proceeding, et al.* (Texas Gulf Coast Area), Docket Nos. AR64-2, *et al.*, 45 FPC 674 (1971).

[3]Commission Opinion No. 639, *Area Rates for the Appalachian and Illinois Basin Areas*, Docket No. R-371, order issued December 12, 1972 (48 FPC ____), rehearing denied February 8, 1973. (49 FPC ____).

(3) The gas will be committed to a new contract; and

(4) The new arrangement will serve to remove Shell as a conduit of any rate increase.

Although the orders in Docket Nos. CI73-450 and CI73-451 were issued separately, their interdependence required that each one be considered with the other in mind, and our order in Docket No. CI73-450 noted that a temporary certificate was being issued concurrently in Docket No. CI73-451. In view of the foregoing, rehearing is not appropriate.

The Commission finds:

AGD's application for rehearing presents no new facts or principles of law which were not fully considered by the Commission in its April 16, 1973, order, or which having been now considered, warrant any modification of that order.

The Commission orders:

The application for rehearing filed by AGD in Docket No. CI73-450 is denied.

By the Commission.

(SEAL)

Kenneth F. Plumb,
Secretary.

UNITED STATES OF AMERICA
FEDERAL POWER COMMISSION

Before Commissioners: John N. Nassikas, Chairman;
Albert B. Brooke, Jr., and Rush Moody, Jr.

Continental Oil Company, *et al.*[1]) FPC Gas Rate Schedule No. 3, *et al.*

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[1]The other producers and rate schedules involved here are listed in the appendix of the April 27 order.

ORDER DENYING REHEARING

(Issued June 1, 1973)

The Public Service Commission for the State of New York (New York) filed on May 2, 1973, an application for rehearing of the Commission's order issued April 27, 1973, in the above-entitled proceedings which accepted certain proposed increased rates to the applicable area new gas ceiling based on the vintaging concepts set forth in Opinion No. 639.

New York in its application for rehearing renews its request that the rate increases in issue here be suspended for a period of at least one day and thereafter be collected subject to refund with interest at 7 percent per annum in the event Opinion No. 639, insofar as it purports to authorize such increases, is reversed, remanded or otherwise set aside upon review. New York also incorporates by reference the reasons set out in its application for rehearing of Opinion No. 639 as to why the vintaging concepts in that opinion are in error.

The merits of the vintaging concepts in Opinion No. 639 were fully discussed in that opinion and the order denying rehearing thereof, as well as in the April 27 order involved here. The reasons for our determination to accept these increases, in lieu of suspending them, despite the fact that New York has sought judicial review of Opinion No. 639, were also discussed in the April 27 order. No further discussion is necessary here.[2]

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[2]Under the vintaging by well commencement date approach adopted in Opinion No. 658, which was issued April 11, 1973, in Docket No. R-425, a producer, as a general rule, would not be permitted for wells commenced on or before December 31, 1972, to collect the rate to be established in Docket No. R-389-B for sales from wells commenced on or after January 1, 1973. But, our action in that case has no bearing on our interpretation of the vintaging provisions contained in area rate opinions where the focal point is the date of the contract covering the sale.

New York's application for rehearing presents no new facts or principles of law which were not fully considered by the Commission in its April 27 order, or, which having now been considered, warrant any modification of that order.

The Commission orders:

The application for rehearing filed by New York on May 2, 1973, is denied.

By the Commission

(SEAL)

Kenneth F. Plumb,
Secretary.

FEDERAL POWER COMMISSION
WASHINGTON, D.C. 20426

IN REPLY REFER TO:
BNG-AC/CA
Docket No. CI73-451
Mobil Oil Corporation
(Operator), et al.

AIRMAIL

April 16, 1973

Mobil Oil Corporation
Three Greenway Plaza East
Suite 800
Houston, Texas 77046
Attention: R.D. Haworth, Esq.

Gentlemen:

Based upon allegations presented in the request for temporary authorization to initiate the sale or transportation of natural gas in interstate commerce pursuant to Section 157.28 of the Commission's Regulations filed in the above entitled proceeding, the Commission finds that an emergency exists, and a temporary certificate is hereby issued to the applicant pursuant to Section 7 of the Natural Gas Act.

This temporary certificate is issued subject to the Commission's Opinion Nos. 595 and 595-A and any further orders issued thereunder and subject to the following express conditions:

(1) The total initial price for the proposed service shall be 24.0¢ per Mcf at 14.65 psia subject to the quality adjustments prescribed in opinion No. 595; *Provided, however,* that the total rate shall in no event exceed the price set forth in the related contract.

(2) The filing, within 90 days from the date of initial delivery of three copies of a Rate Schedule-Quality Statement as specified by ordering paragraph (D) of Commission's Opinion No. 595, reflecting the rate determined in (1) herein.

(3) Section 154.93(b-1) of the Commission's Regulations is hereby waived to permit the inclusion in the related rate schedule of the contractual provision for rate increases to a higher area rate found to be proper by hearing, rulemaking or a Commission approved settlement.

(4) Mobil's request that the price authorized in (1) above be effective as of August 21, 1972, is hereby denied; such price will be effective for all sales made on or after the date of initial delivery under the authorization granted herein.

(5) Your acceptance or rejection of the temporary certificate may be filed within 30 days of the date hereof. If accepted, the temporary certificate shall be effective upon the date of receipt of the acceptance by the Secretary. If no acceptance or rejection has been filed within 30 days, the temporary certificate shall

be deemed to have been accepted and shall be effective on that date. However, the temporary authorization will not be effective until such time as the purchaser or transporter of the natural gas to be sold thereunder is authorized to construct and operate such facilities as may be necessary to receive and transport the gas. Service under this temporary certificate shall commence within 90 days of the issuance thereof. Such service may not be discontinued without permission of the Commission issued pursuant to the provisions of the Natural Gas Act whether the contract term has expired or not. If reconsideration of the temporary certificate is sought, service hereunder shall not commence pending final action of the Commission thereon.

The related proposed rate schedule is hereby accepted for filing to be effective on the date of initial delivery, subject to the provisions of Sections 154.94(c) and 154.101 of the Commission's Regulations under the Natural Gas Act.

The rate schedule has been designated as follows:

Description	Designation
Contract 11-25-71	Mobil Oil Corporation (Operator), et al. FPC Gas Rate Schedule No. 492

Please advise the Commission of the date of commencement of deliveries under such rate schedule, making reference in your communication to the rate schedule as designated above.

The issuance of this temporary certificate and the acceptance of the above rate schedule are without prejudice to such final disposition of the application for certificate as the record may require.

By direction of the Commission.

Secretary

cc: Texas Eastern Transmission Corporation
P. O. Box 1612
Shreveport, Louisiana 71130

Appendix C

RATES AND CHARGES; SCHEDULES; SUSPENSION OF NEW RATES

SEC. 4. (a) All rates and charges made, demanded, or received by any natural-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) No natural-gas company shall, with respect to any transportation or sale of natural gas subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission, within such time (not less than sixty days from the date this act takes effect) and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showing all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulations, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days'

notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, State commission, or gas distributing company [1a] or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect; [1a] and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of the suspension period, on motion of the natural-gas company making the filing, the proposed change of rate, charge, classification, or service shall go into effect. Where increased rates or charges are thus made effective, the Commission may, by order, require the natural-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts were paid, and, upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the

natural-gas company, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible. [52 Stat. 822 (1938); 76 Stat. 72 (1962); 15 U.S.C. § 717c]

FIXING RATE AND CHARGES; DETERMINATION OF COST OF PRODUCTION OR TRANSPORTATION

SEC. 5. (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State, municipality, State commission, or gas distributing company, shall find that any rate, charge, or classification demanded, observed, charged, or collected by any natural-gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however*, That the Commission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural-gas company on file with the Commission, unless such increase is in accordance with a new schedule filed by such natural-gas company; but the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.

(b) The Commission upon its own motion, or upon the request of any State commission, whenever it can do so without prejudice to the efficient and proper conduct of its affairs, may investigate and determine the cost of the production or transportation of natural gas by a natural-gas company in cases where the Commission has no authority to establish a rate governing the transportation or sale of such natural gas. [52 Stat. 823 (1938); 15 U. S. C. § 717d]

REHEARING; COURT REVIEW OF ORDERS

SEC. 19 (a) [9] Any person, State, municipality, or State commission aggrieved by an order issued by the Commission in a proceeding under this act to which such person, State, municipality, or State commission is a party may apply for a rehearing within thirty days after the issuance of such order. The application for rehearing shall set forth specifically the ground or grounds upon which such application is based. Upon such application the Commission shall have power to grant or deny rehearing or to abrogate or modify its order without further hearing. Unless the Commission acts upon the application for rehearing within thirty days after it is filed, such application may be deemed to have been denied. No proceeding to review any order of the Commission shall be brought by any person unless such person shall have made application to the Commission for a rehearing thereon. Until the record in a proceeding shall have been filed in a court of appeals, as provided in subsection (b), the Commission may at any time, upon reasonable notice and in such manner as it shall deem proper, modify or set aside, in whole or in part, any finding or order made or issued by it under the provisions of this Act.

(b) [9] Any party to a proceeding under this act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States [10] for any circuit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be transmitted by the clerk of the court to any member of the Commission and thereupon the Commission shall file with the court the record upon which

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[9] The Act of August 28, 1958 (72 Stat. 941 at 947) added the last sentence to subsection (a) and, in the second sentence of subsection (b), substituted "Transmitted by the clerk of the court to" for "served upon", substituted "file with the court" for "certify and file with the court a transcript of" inserted "as provided in section 2112 of title 28, United States Code", and, in the third sentence, substituted "jurisdiction, which upon the filing of the record with it shall be exclusive" for "exclusive jurisdiction".

[10] Circuit Court of Appeals of the United States was redesignated as "United States Court of Appeals" by Act of June 25, 1948, 62 Stat. 870.

the order complained of was entered, as provided in section 2112 of title 28, United States Code. Upon the filing of such petition such court shall have jurisdiction, which upon the filing of the record with it shall be exclusive, to affirm, modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in [former] sections 239 and 240 of the Judicial Code, as amended (U.S.C., title 28, sec. 1254).

(c) The filing of an application for rehearing under subsection (a) shall not, unless specifically ordered by the Commission, operate as a stay of the Commission's order. The commencement of proceedings under subsection (b) of this section shall not, unless specifically ordered by the court, operate as a stay of the Commission's order. [52 Stat. 831 (1938); 15 U. S. C. § 717r]

Supreme Court, U. S.
FILED
AUG 31 1976
MICHAEL RODAK, JR., CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1975

No. 75–1565

ASSOCIATED GAS DISTRIBUTORS,

Petitioner,

v.

FEDERAL POWER COMMISSION

Respondent.

REPLY BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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August 31, 1976

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ASSOCIATED GAS DISTRIBUTORS,

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Respondent.

REPLY BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

Respondents' Oppositions to the Petitions for Certiorari contain two fatal flaws. First, respondents' vigorous defense of F.P.C. Opinion No. 639 is irrelevant. The issue presented in this Petition is not the wisdom or legality of the F.P.C.'s

basic decision (in Opinion No. 639) gradually to abolish the vintaging concept in producer ratemaking. We concede that the Commission is free, indeed it may be obliged, to overhaul its pricing policies to provide additional gas supply incentives or remove disincentives. But, the problem here is that the rate increases at bar do not serve the gas supply objectives at which the Opinion No. 639 policy was aimed. A significant increase in the rate allowed for gas production already permanently committed to the interstate market, without more, has no impact whatsoever on gas supply. Nothing in respondents' memoranda suggests how these rate orders will yield the consumer any added gas supply. It is the Commission's gross default in implementing its supply-improvement policy which invalidates the orders at bar. Judge Robinson's dissenting opinion below pinpoints the distinction between the validity of these orders and the Opinion No. 639 policy (upheld by the Fifth Circuit in the *Shell* case) in the following passage:

> The orders are clearly of the type which *Shell* referred to in its call for substantial evidence to support the absence of a vintaging component from their rate structures. I agree with the Fifth Circuit that that absence is an essential element of the orders, and as such depended on an ample evidentiary foundation for survival. The majority position here, in treating supporting evidence as an unnecessary commodity, not only disregards *Shell's* specific ruling on the point but, more fundamentally, also ignores the Supreme Court's mandate on that score. Appendix A, AGD's Petition at 37-38 (footnotes omitted).

Second, the rationale given by the Commission for Opinion No. 639 and hence the orders here, i.e., the need to abolish price vintaging in the interest of supply improvement, has

now been thoroughly discredited by the Commission itself. This is evident from the action taken by the Commission on July 27, 1976 in its Opinion No. 770.[1]

In Opinion No. 770 the Commission has "reinterpreted" its previous renewal contracts interpretation to restore price vintaging as a basic component of producer rate regulation. Rather than seeking to abolish the concept of vintaging, the Commisison has instead found it necessary to prescribe *four* vintages of gas for ratemaking purposes in Opinion No. 770. The Commission therefore cannot justify either its renewal contracts policy or its implementation thereof in the instant orders on the grounds that it is properly moving toward the gradual abolition of vintaging. Without the "gradual abolition" policy justification, the rate orders herein fall of their own weight. The Commission's action in Opinion No. 770 deprives the "gradual abolition of vintaging" premise of its presumptive validity and exposes the instant orders as unjustified and unlawful.

Were it not for the significant cost consequences of Opinion No. 639 rate increases to consumers in the interstate markets, the Commission's policy reversal might be excusable insofar as these cases are concerned. As indicated in AGD's Petition, however, these orders all illustrative of a large number of F.P.C. orders of substantially identical character which have been held in abeyance by the court below pending the final disposition here. Together, these orders permit the collection of millions of dollars annually.

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[1] *National Rates for Jurisdictional Sales to Natural Gas Dedicated to Interstate Commerce on or After January 1, 1973, For the Period January 1, 1975, to December 31, 1976* (F.P.C., July 27, 1976). The relevant portion of this Opinion is excerpted in the August 16, 1976 Reply Memorandum filed by the Public Service Commission of the State of New York in No. 75-1556.

CONCLUSION

For these reasons, AGD submits that the Court should grant the Petition in these cases and remand them to the court below with instructions to set aside the orders in question and remand the proceedings to the Commission for further proceedings in which the producers are required either to demonstrate the availability of additional gas supply to the interstate market commensurate with the increased revenue derived from these orders or make refunds.

Respectfully submitted,

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August 31, 1976